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ORIGINAL


# ELLIOTT & ELLIOTT, P.A.

ATTORNEYS AT LAW

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COLUMBIA, SOUTH CAROLINA 29205

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SCOTT ELLIOTT

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April 19, 2007

COPY

Posted: D. Duke

Dept: SA

Date: 4-20-07

Time: 7:35

2007 APR 19 PM 4: 14

SC PUBLIC SERVICE COMMISSION

RECEIVED

VIA HAND DELIVERY

Charles L. A. Terreni, Esquire
Chief Clerk and Administrator
South Carolina Public Service Commission
101 Executive Center Drive
Columbia, SC 29210

RE: Application of Inter-Tel Netsolutions, Inc. for a Certificate and Necessity to Provide Local Exchange Telecommunication Services and Local Service Offerings to be Regulated in Accordance with Procedures Authorized for NewSouth Communications in Order No. 98-165 in Docket No. 97-467-C.

Dear Mr. Terreni:

Enclosed please find for filing an original and fifteen (15) copies of the Application of Inter-Tel Netsolutions, Inc. for Authority to Provide Resold and Facilities-Based/UNE Local Exchange Service. By copy I am serving the Office of Regulatory Staff.

I have enclosed an extra copy of this application which I would ask you to date stamp and return to me through my courier. If you have any questions or if I may provide you with any additional information, please do not hesitate to contact me. Thank you.

Sincerely,

Elliott & Elliott, P.A.

Scott Elliott

SE/jcl

Enclosures

cc: Lance J.M. Steinhart, Esquire

ORIGINAL

STATE OF SOUTH CAROLINA
BEFORE THE SOUTH CAROLINA PUBLIC SERVICE COMMISSION

**In re:**

**Application of**
**INTER-TEL NETSOLUTIONS, INC.**
**For a Certificate of Public Convenience and Necessity to Provide Local Exchange Telecommunications Services and for local service offerings to be regulated in accordance with procedures authorized for NewSouth Communications in Order No. 98-165 in docket No. 97-467-C.**

**DOCKET NO.** 2007-155-C

RECEIVED
2007 APR 19 PM 4:14
SC PUBLIC SERVICE COMMISSION

**APPLICATION OF INTER-TEL NETSOLUTIONS, INC.**

**FOR AUTHORITY TO PROVIDE RESOLD AND FACILITIES-BASED/UNE**

**LOCAL EXCHANGE SERVICE**

Inter-Tel NetSolutions, Inc. ("Inter-Tel" or "Applicant"), pursuant to S.C. Code Ann. § 56-9-280(B)[1] and Section 253 of the Telecommunications Act of 1996[2], respectfully submits this Application for Authority to Provide Resold Local Exchange Service ("Application") in the State of South Carolina and for local service offerings to be regulated in accordance with procedures authorized for NewSouth Communications in Order No. 98-165 in docket No. 97-467-C.

---

[1] As amended by Act No. 354, signed by the Governor on June 6, 1996.

[2] Telecommunications Act of 1996, 47 U.S.C. § 253 (1996).

Inter-Tel intends to provide local exchange service to customers located in non-rural local exchange carriers' service areas of South Carolina. Should its Application be granted, Inter-Tel plans to commence offering service immediately upon the establishment of the appropriate resale arrangements with facilities-based carriers. Applicant intends to utilize MCI, AT&T and XO Communications, and other equivalent providers as its underlying carriers.

Approval of this Application will promote the public interest by increasing the level of competition in the South Carolina telecommunications market. Ultimately, competition will compel all telecommunications service providers to operate more efficiently and pass the resultant cost savings on to consumers. In addition, as a result of competition, the overall quality of local exchange service will improve.

In support of its Application, Inter-Tel states as follows:

## I. Introduction

1. The name and address of the Applicant are:
   INTER-TEL NETSOLUTIONS, INC.
   4310 East Cotton Center Blvd., Suite A-100
   Phoenix, Arizona 85040

2. All correspondence, notices, inquiries and other communications regarding this Application should be directed to:

| | |
|---|---|
| Lance J.M. Steinhart | Local Counsel: |
| Lance J.M. Steinhart, PC | Scott Elliott, Esq. |
| 1720 Windward Concourse, Ste. 250 | Elliott & Elliott, P.A. |
| Alpharetta, Georgia 30005 | 721 Olive Street |
| Telephone: 770/232-9200 | Columbia, SC 29205 |
| Facsimile: 770/232-9208 | Telephone: 803/771-0555 |
| Email: lsteinhart@telecomcounsel.com | Facsimile: 803/771-8010 |

3. In support of this Application, the following exhibits are attached hereto:

   a. Exhibit A - Inter-Tel's Articles of Incorporation filed with the Secretary of State for the State of Texas;

b. Exhibit B - Inter-Tel's Certificate of Authority to Operate in South Carolina as a Foreign Corporation;
c. Exhibit C - Inter-Tel, Inc.'s Form 10-Q for the quarter ended June 30, 2006.
d. Exhibit D - Biographies of selected Inter-Tel management;
e. Exhibit E - Proposed Tariff

## II. Description of the Applicant

### 1. General Information

Applicant is a Texas Corporation, which was formed on June 19, 1990. The company is headquartered at 4310 East Cotton Center Blvd., Suite A-100, Phoenix, Arizona 85040.

### 2. Customer Service

Inter-Tel's customer service representatives are available to assist its customers and will promptly respond to all customer inquiries. Customers may call (800) 821-1661 or a local number. The applicable toll free or local numbers will be printed on customers' monthly billing statements. Alternately, customers wishing to communicate with an Inter-Tel customer service representative in writing may send written correspondence to Inter-Tel at:

Inter-Tel NetSolutions, Inc.
ATTN: Customer Service
4310 East Cotton Center Blvd., Suite A-100
Phoenix, Arizona 85040

Inter-Tel's customer service representatives are prepared to respond to a broad range of service matters, including inquiries regarding: (1) the types of services offered by Inter-Tel and the rates associated with such services; (2) monthly billing statements; (3) problems or concerns pertaining to a customer's current service; and (4) general service matters.

## III. Inter-Tel Possesses the Technical, Managerial and Financial Expertise Necessary to Provide Local Exchange Service

Inter-Tel possesses the requisite technical, financial and managerial capabilities to operate as a competitive telecommunications provider. These capabilities are explained in detail below.

### 1. Financial Qualifications

Inter-Tel is financially able to provide the services proposed in its tariff as evidenced by its parent company's Form 10-Q for the quarter ended June 30, 2006.

### 2. Managerial Qualifications

Inter-Tel's senior management team is highly skilled, having acquired considerable experience in the telecommunications industry. Using this extensive expertise, Inter-Tel's management team has developed innovative marketing strategies. In conjunction with effective financial and operational measures, these marketing strategies will enable the company to provide quality service at competitive rates, while resulting in profitable operations for the Applicant. Inter-Tel has extensive experience in the technical, managerial, and financial aspects of the telecommunications industry.

### 3. Technical Qualifications

Applicant's key management personnel have significant business and telecommunications experience. Applicant will also rely upon the technical expertise and telecommunications experience of its underlying carriers. Applicant is currently authorized to provide local exchange service in Arizona, California, Colorado, Florida, Georgia, Illinois, Kansas, Minnesota, Missouri, Nevada, New Jersey, New York, Pennsylvania, Tennessee, Texas and Washington and authorized to provide interexchange services throughout the United States. Applicant is in the process of applying for authorization to provide competitive local exchange in approximately 20 additional states. Applicant has not been denied authority for any of the services for which it seeks authority in this Application. Applicant is currently providing long distance service in throughout the United States, and is providing local exchange service in Arizona, California, Colorado, Florida, Georgia, Illinois, Kansas, Minnesota, Missouri, Nevada, New Jersey, New York, Pennsylvania, Tennessee, Texas and Washington.

Inter-Tel will resell local exchange services, utilizing the facilities of the existing of incumbent local exchange carriers ("LECs") or underlying carriers that presently serve South Carolina.

APPLICANT seeks authority to resell local exchange services throughout the State primarily in the areas served by Bellsouth. Applicant's local calling areas initially will coincide with the incumbent local exchange carrier's local calling areas. Its services will be available on a full-time basis, twenty-four hours a day, seven days a week, to customers within the geographic boundaries of the State of South Carolina. Customers will be billed by APPLICANT. Applicant is committed to providing access to a local operator, directory assistance, 911 services, and dual relay services. Applicant is also willing to accept its obligations to collect 911 and dual relay service surcharges from its local exchange customers, and to remit those funds to the appropriate authorities.

As the foregoing illustrates, Inter-Tel possesses considerable telecommunications expertise. Inter-Tel asserts that it is technically qualified to provide local exchange telecommunications services in South Carolina.

## IV. Approval of Inter-Tel's Application is in the Public Interest

Granting Inter-Tel's Application is consistent with S.C. Code Ann. § 58-9-280(B), as amended by 1996 Act No. 354, and, in that regard Applicant makes the following representations to the Commission:

a. Applicant possesses the technical, financial, and managerial resources sufficient to provide the services requested;

b. Applicant's services will meet the service standards required by the Commission;

c. The provision of local service by Applicant will not adversely impact the availability of affordable local service;

d. Applicant, to the extent it is required to do so by the Commission, will participate in the support of universally available telephone service at affordable rates; and,

e. The provision of local service by Applicant will not adversely impact the public interest.

The demands of a competitive market are a better means to achieve affordability and quality of service than a monopoly environment. As competitors vie for market share, they will compete based upon price, innovation and customer service.

Those providers trust that offer consumers the most cost effective products will gain market share. In contrast, providers whose products do not meet the needs of consumers will lose market share and, ultimately, be eliminated from the industry.

Additionally, Inter-Tel's entry into the local exchange markets will not unreasonably prejudice or disadvantage any telephone service providers. Incumbent local exchange carriers presently serve a large majority of the local exchange customers in South Carolina. The major advantages of incumbency (i.e., ownership of the existing local network as well as access to, and long-standing relationships with, every local customer) constitute a substantial obstacle to new entrants. Moreover, exchange services competition will stimulate the demand for the services supplied by all local service carriers, including those of the incumbent LECs. Thus, in a competitive market, there will be increased potential for such LECs to generate higher revenues. Additionally, in a competitive market, incumbent providers will have market incentives to improve the efficiency of their operations, thereby reducing their costs and ultimately their profit margins. Finally, it is important to recognize that in a competitive market, incumbent LECs will derive revenues from both resellers of their local exchange services as well as facilities based competitive local exchange providers.

Currently, South Carolina consumers have a limited choice with regard to the provision of local exchange telecommunications service. A competitive local service market comprised of incumbents and competitive providers such as Inter-Tel will offer consumers a competitive option and, therefore, will better satisfy the needs of various market segments. In this regard, approval of this Application is clearly in the public interest.

## V. Description of Services Offered and Service Territory

Inter-Tel expects to offer a full array of services to customers, including the following:

Local Exchange:

A. Local Exchange Services for customers that will enable customers to originate and terminate local calls in the local calling area served by other LECs, including local dial tone and custom calling features.

B. Switched local exchange services, including basic service, trunks, carrier access, and any other switched local services that currently exist or will exist in the future.

C. Non-switched local services (e.g., private line) that currently exist or will exist in the future.

D. Centrex and/or Centrex-like services that currently exist or will exist in the future.

E. Digital subscriber line, ISDN, and other high capacity services.

Applicant submits contemporaneously with this application its proposed tariff for local exchange service (Exhibit E), which contains a description of services to be provided, all rules and regulations applicable to such services, and proposed rates for such services.

## VI. Waivers and Regulatory Compliance

Inter-Tel requests that the Commission grant it a waiver of those regulatory requirements inapplicable to competitive local service resellers such as Inter-Tel. Such rules are not appropriate or necessary for competitive providers and constitute an economic barrier to entry into the local exchange market.

### 1. Financial Record-Keeping System

a. Inter-Tel respectfully requests that it be exempt from any record-keeping rules or regulations that might require a carrier to maintain its financial records in conformance with the Uniform System of Accounts ("USOA"). The USOA was developed by the FCC as a means of regulating telecommunications companies subject to rate base regulation.

b. As a competitive carrier, Inter-Tel maintains its book of accounts in accordance with Generally Accepted Accounting Principles ("GAAP"). Neither the FCC, nor the Commission, has required Inter-Tel to maintain its records under the USOA for purposes of Inter-Tel's operations. Thus, Inter-Tel does not possess the detailed cost data required by USOA, nor does it maintain detailed records on a state-specific basis. As a competitive provider, Inter-Tel's network operations are integrated to achieve maximum efficiency. Having to maintain records pertaining specifically to its South Carolina local service operations would place an extreme burden on Inter-Tel.

c. Moreover, Inter-Tel asserts that because it utilizes GAAP, the Commission will have a reliable means by which to evaluate Inter-Tel's operations. Therefore, Inter-Tel hereby respectfully requests to be exempt from the any USOA requirements of the Commission.

d. In addition, the Company hereby respectfully requests a waiver of 26 S.C. Code & Ann. Regs. 103-610, which requires books and records to be kept in the State of South Carolina, but rather, the Company desires to keep its books and records at its principal place of business.

**2. Local Exchange Directories**

Applicant respectfully requests a waiver of the requirement in Rule 103-631 to publish and distribute local exchange directories. Inter-Tel will make arrangements with the incumbent LECs whereby the names of Inter-Tel's customers will be included in the directories published by the incumbent LECs. LEC directories will also be modified to include Inter-Tel's customer service number. These directories will be distributed to Inter-Tel's customers. This approach is entirely reasonable and will have a direct benefit to the customers of both Inter-Tel and the incumbent LEC since they need only refer to one directory for a universal listing of customer information. It would be an unnecessary burden on Inter-Tel to require that it publish and distribute its own directory to all customers located within each exchange area, particularly since nearly all of these customers will be customers of the incumbent LECs. It is more efficient for Inter-Tel to simply include its limited customer list in the existing directories of the incumbent LECs.

**3. Flexible Regulation of Local Services**

Applicant respectfully requests that its local service offerings be regulated in accordance with procedures authorized for NewSouth Communications in Order No. 98-165 in docket No. 97-467-C.

**4. Marketing Practices**

Pursuant to the South Carolina Public Service commission's Order No. 95-658 (issued March 20, 1995), Applicant makes the following affirmation relating to the Applicant's provision of services:

As a telephone utility under the regulation of the Public Service Commission of South Carolina, Carrier does hereby assert and affirm that as a reseller of intrastate telecommunications service, Carrier will not indulge or participate in deceptive or misleading telecommunications marketing practices to the detriment of consumers in South Carolina, and will comply with those marketing procedures, if any, set forth by the Public Service Commission. Additionally, Carrier will be responsible for the marketing practices of its contracted telemarketers for compliance with this provision. Carrier understands that violation of this provision could result in a rule to show cause as to the withdrawal of its certification to complete intrastate telecommunications traffic within the state of South Carolina.

**5. Maps**

Applicant's local exchange calling areas will initially mirror the service areas of the incumbent local exchange carriers; therefore, Applicant hereby respectfully requests a waiver of the map-filing requirement pursuant to Commission Rule 103-612.2.3.

## VII. Conclusion

This Application demonstrates that INTER-TEL NETSOLUTIONS, INC. possesses the technical, financial and managerial resources to provide resold and facilities-based/UNE local exchange service in the State of South Carolina. Furthermore, granting this Application will promote the public interest by increasing the level of competition in the South Carolina telecommunications market. Ultimately, competition will compel all exchange telecommunications service providers to operate more efficiently and pass the resultant cost savings on to consumers. In addition, as a result of competition, the overall quality of local exchange service will improve. As stated above, Applicant does not intend to provide local service, by its own facilities or otherwise, to any customer located in a rural incumbent LEC's service area, until Applicant provides such LECs notice of intent at least 30 days prior to the date of the intended service.

Wherefore, INTER-TEL NETSOLUTIONS, INC., respectfully petitions this Commission for authority to operate as a reseller of local exchange telecommunications services in the State of South Carolina and for local service offerings to be regulated in accordance with procedures authorized for NewSouth Communications in Order No. 98-165 in docket No. 97-467-C, in accordance with this Application and for such other relief as it deems necessary and appropriate.

Respectfully submitted,

**Inter-Tel NetSolutions, Inc.**

______________________________

Lance J.M. Steinhart
Lance J.M. Steinhart, PC
1720 Windward Concourse, Suite 250
Alpharetta, Georgia 30005
(770) 232-9200/Phone
(770) 232-9208/Fax
lsteinhart@telecomcounsel.com

and

______________________________

Scott Elliott
721 Olive Street
Columbia, SC 29205
(803) 771-0555

***Attorneys for Applicant***

April 18, 2007 ~~, 2006~~

## VERIFICATION OF APPLICANT

I, Jon Brinton, Vice-President and General Manager to Inter-Tel NetSolutions, Inc., a Texas Corporation, the applicant for a Certificate of Public Convenience and Necessity from the Public Service Commission of the State of South Carolina, verify that based on information and belief, I have knowledge of the statements in the foregoing Application, and I declare that they are true and correct.

Jon Brinton
Vice-President and General Manager
Inter-Tel NetSolutions, Inc.

Sworn to me, the undersigned
Notary Public on this
21st day of November, 2006.

OFFICIAL SEAL
W. W. FOSTER
NOTARY PUBLIC-ARIZONA
MARICOPA COUNTY
My Comm. Expires June 12, 2008

State of Arizona
County of Maricopa

Notary Public

# EXHIBIT "A"
# ARTICLES OF INCORPORATION

## ARTICLES OF INCORPORATION

## OF

## INTER-TEL NETSOLUTIONS, INC.

FILED
In the Office of the
Secretary of State of Texas

JUN 1 9 1998

Corporations Section

I, the undersigned natural person of the age of twenty-one (21) years or more, a citizen of the State of Texas, acting as an Incorporator of a corporation (hereinafter referred to as the "Corporation"), under the Texas Business Corporation Act (hereinafter referred to as the "Act"), do hereby adopt the following Articles of Incorporation for such Corporation:

### ARTICLE ONE

### INTER-TEL NETSOLUTIONS, INC.

The name of the Corporation is Inter-Tel NetSolutions, Inc.

### ARTICLE TWO

### Duration

The period of existence of the Corporation is perpetual.

### ARTICLE THREE

### Purposes and Powers

Section 3.01 Purposes and Powers in Addition to Statutory Powers: The purposes for which the Corporation is organized, and the powers, in addition to the general powers conferred by the Act, which the Corporation shall be entitled to exercise, all subject to the limiting provisions set forth in Section 3.03 of this Article are:

(a) To buy, sell, exchange, use and/or otherwise transfer telecommunication services, including but not limited to, equipment and long distance services.

(b) To engage in and transact all business and all activities for which a corporation may be properly organized and operated under the Act and subject to the provisions of the Texas Miscellaneous Corporation Laws Act.

(c) To have and exercise all powers which may be granted to corporations organized under the Act and subject to the provisions of the Act, whether granted by these Articles or construction of law.

Section 3.02. Direction of Purpose and Exercise of Powers of Directors: Subject to any limitations or restrictions imposed by the Act, by any other law, or by these Articles of Incorporation, the Board of Directors hereby is authorized to direct the purposes set forth in this Article and to exercise all the powers of the Corporation without previous authorization or subsequent approval by the Shareholders; and all parties dealing with the Corporation shall have the right to rely on any action taken by the Corporation pursuant to such action by the Board of Directors.

Section 3.03. Limiting Provisions: Nothing in these Articles of Incorporation is to be construed as authorizing or attempting to authorize the Corporation:

(a) To transact any business in the State of Texas expressly prohibited by any law of the State of Texas;

(b) To engage in any activity in the State of Texas which cannot lawfully be engaged in without first obtaining a license under the laws of the State of Texas, and which license cannot be granted to a corporation;

(c) To take any action in violation of the Anti-Trust laws of the State of Texas; or,

(d) To take any action in violation of Part Four of the Texas Miscellaneous Corporation Laws Act.

## ARTICLE FOUR

### Authorized Shares

The aggregate number of shares which the Corporation shall have authority to issue is One Million (1,000,000) shares, with a par value of One Dollar ($1.00) per share, all of which shares shall be known as "Common Stock".

ARTICLE FIVE

Initial Consideration for Issuance of Shares

The Corporation will not commence or transact any business or incur any indebtedness except such as shall be incidental to this organization or to obtaining subscriptions to or payment for its shares, until it has received for the issuance of its shares consideration of the value of at least ONE THOUSAND AND NO/100 DOLLARS ($1,000.00), consisting of money, labor done or property actually received.

ARTICLE SIX

Rights of Directors and Officers

to Deal with Corporation

No Director and no Officer of the Corporation shall be disqualified by reason of his office from dealing with or contracting with the Corporation either as vendor, seller, purchaser, vendee, buyer, mortgagee, mortgagor, or otherwise; and no transaction of this Corporation shall be void or voidable by reason of the fact that the Director or Officer of any firm in which a Director or Officer of this Corporation is a member, or any corporation of which a Director or Officer of this Corporation is a shareholder or a director or officer, is in any way interested in such transaction.

## ARTICLE SEVEN

### Denial of Preemptive Rights

No shareholder shall be entitled, as a matter of right, to subscribe for, purchase or receive any shares of stock or any rights or options of the Corporation which it may issue or sell, whether out of the number of shares authorized by these Articles of Incorporation or by amendment thereof, or out of the shares of the stock of the Corporation acquired by it after the issuance thereof, nor shall any shareholder be entitled, as a matter of right, to subscribe for, purchase or receive any bonds, debentures or other securities which the Corporation may issue or sell that shall be convertible into, or exchangeable for, stock, or to which shall be attached or appertain to any warrant or warrants or other instrument or instruments that shall confer upon the holder or owner of such obligations the right to subscribe for, purchase or receive from the Corporation any shares of its authorized capital stock; but all such additional issues of stock, rights and options or of bonds, debentures or other securities convertible into, or exchangeable for, stock or to which warrants shall be attached or appertain or which shall confer upon the holder the right to subscribe for, purchase or receive any shares of stock, may be issued, optioned for, and sold or disposed of by the Corporation pursuant to resolution of its Board of Directors to such persons, firms or corporations and upon such terms as may be lawful and may to such Board of Directors seem proper and advisable, without first offering such stock or securities or any part thereof to the shareholders. The acceptance of stock in the Corporation shall be a waiver of any preemptive rights or preferential rights which, in the absence of this provision might otherwise be asserted by shareholders of the Corporation or any of them.

ARTICLE EIGHT

Prohibition of Cumulative Voting

At each election for Directors, every shareholder entitled to vote at such election shall have the right to vote, in person or by proxy, the number of shares owned by him for as many persons as there are Directors to be elected and for whose election he has the right to vote, but it is expressly prohibited for any shareholder to cumulate his votes by giving one candidate as many votes as the number of such Directors multiplied by his shares shall equal, or by distributing such votes on such principle among any number of such candidates.

ARTICLE NINE

Provisions for Regulation of the Corporation and its Internal Affairs

The following provisions are set forth for the regulation of the Corporation and its internal affairs to the extent that such provisions are not inconsistent with the law:

Section 9.01. Bylaws: The power to alter, amend or repeal the bylaws and to adopt new bylaws shall be vested in the Board of Directors and in the shareholders entitled to vote for the election of Directors; provided, however, that any bylaw or amendment thereto as adopted by the Board of Directors may be altered, amended or repealed, or a new bylaw in lieu thereof maybe adopted, by vote of such shareholders; but no bylaw which has been altered, amended, or adopted by vote of such shareholders may be altered, amended or repealed by the Board of Directors, nor may the substance of any bylaw repealed by vote of such shareholders be again adopted by the Board of Directors, until one year shall have expired since such action by vote of such shareholders.

Section 9.02. Other Provisions: Other provisions for the regulation of the Corporation and its internal affairs not inconsistent with law or these Articles of Incorporation may be set forth in the bylaws, including but not limited to, provisions regulating and providing for compensation of directors, interest of directors in contracts, provisions for working capital, liability and indemnification of directors, officers and employees, and voting of shares by proxy. All rights of the shareholders, directors, officers, agent and employees of the Corporation shall be deemed subject to all provisions of the bylaws to the fullest extent permitted by law.

ARTICLE TEN

Initial Registered Office and Agent

The post office address of the initial registered office of the Corporation is Houston, Texas, and the name of the initial registered agent of the Corporation is Steven P. Nichols, 4900 Langfield Road, Houston, Texas 77040.

ARTICLE ELEVEN

Directors

Section 11.01. Number: The Board of Directors of the Corporation shall consist of three (3) members. The number of Directors shall be fixed by the bylaws and may be increased or decreased by amendment of the bylaws; but no decrease shall have the effect of shortening the terms of any incumbent Director. In the absence of a bylaw fixing the number of Directors, the number shall be identical to the number of initial Directors.

Section 11.02. Qualifications: The Directors need not be residents of the State of Texas or shareholders of the Corporation.

Section 11.03. Initial Directors: The number, names, and addresses of the persons who are to serve as Directors until the first annual meeting of the shareholders, or until their successors are elected and qualified, are:

Steven G. Mihaylo
6505 West Chandler Boulevard
Chandler, Arizona 85226

Ralph Marsh
6505 West Chandler Boulevard
Chandler, Arizona 85226

Steven Prescott Nichols
4900 Langfield Road
Houston, Texas 77040

## ARTICLE TWELVE

### Incorporator

The name and address of the Incorporator of the Corporation is:

John L. Gardner
9301 Southwest Freeway
Suite 225
Houston, Texas 77074

IN WITNESS WHEREOF, I have hereunto set my hand this the 12th day of June 1990.

JOHN L. GARDNER

THE STATE OF TEXAS §
§
COUNTY OF HARRIS §

I, the undersigned authority, a Notary Public in and for said County and State, do hereby certify that on this the 12th day of June 1990, personally appeared before me, John L. Gardner, who, being by me first duly sworn, declared that he is the person who signed the foregoing instrument as Incorporator, and that the statements therein contained are true.

Nina T. Berkley
Notary Public in and for
HARRIS COUNTY, T E X A S

Nina T. Berkley
Printed Name of Notary

\intertel\netsolutions.aoi

My Commission Expires: 12/11/93

**EXHIBIT "B"**
**FOREIGN CORPORATION QUALIFICATION**

# Secretary of State Search
## Mark Hammond's Office



**Office of the South Carolina Secretary of State**

Business Filings Division

**Information for:** **INTER-TEL NETSOLUTIONS, INC.**

Check Cha

Note*** This online database was last updated on 12/19/2006 see our Disclaimer

| | |
|---|---|
| **DOMESTIC / FOREIGN:** | Foreign |
| **STATUS:** | Reinstatement |
| **STATE OF INCORPORATION / ORGANIZATION:** | TEXAS |
| | **For Profit** |

### REGISTERED AGENT INFORMATION

| | |
|---|---|
| **REGISTERED AGENT NAME:** | CORPORATION SERVICE COMPANY |
| **ADDRESS:** | 5000 THURMOND MALL BLVD |
| **CITY:** | COLUMBIA |
| **STATE:** | SC |
| **ZIP:** | 29201 0000 |
| **SECOND ADDRESS:** | |

| | |
|---|---|
| **FILE DATE:** | 07/22/1996 |
| **EFFECTIVE DATE:** | 07/22/1996 |
| **DISSOLVED DATE:** | |

**CORPORATION HISTORY RECORDS**

| Code | File Date | Comment |
|---|---|---|
| REINSTATEMENT | 04/26/2004 | REINSTATEMENT |
| Agent | 09/18/2002 | CH REG ADD |
| FORFEITURE | 09/24/1997 | AUTH REVOKED #2 |
| AUTHORITY(FOREIGN)) | 07/22/1996 | AUTHORITY |

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## EXHIBIT "C"
## FINANCIAL INFORMATION

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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION
**Washington, D.C. 20549**

# FORM 10-Q

**QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarter ended June 30, 2006**

**Commission File Number: 0-10211**

# INTER-TEL (DELAWARE), INCORPORATED

Incorporated in the State of Delaware I.R.S. No. 86-0220994

**1615 S. 52nd Street**
**Tempe, Arizona 85281**
**(480) 449-8900**

| Title of Class | Outstanding as of June 30, 2006 |
|---|---|
| Common Stock, par value $0.001 | 26,621,991 |

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one)

Large Accelerated filer ☐ Accelerated filer ☑ Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes. ☐ No. ☑

# INDEX

## INTER-TEL (DELAWARE), INCORPORATED AND SUBSIDIARIES

Table of Contents

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
INTER-TEL (DELAWARE), INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

| (in thousands, except share amounts) | June 30, 2006 (Unaudited) | December 31, 2005 (Note A) |
|---|---|---|
| **ASSETS** | | |
| **CURRENT ASSETS** | | |
| Cash and equivalents | $116,032 | $103,774 |
| Short-term investments | 63,881 | 63,689 |
| **TOTAL CASH AND SHORT-TERM INVESTMENTS** | 179,913 | 167,463 |
| Accounts receivable, net of allowances of $6,319 in 2006 and $6,235 in 2005 | 49,586 | 44,072 |
| Inventories | 22,267 | 19,644 |
| Net investment in sales-leases, net of allowances of $900 in 2006 and $998 in 2005 | 17,497 | 19,699 |
| Income taxes receivable | — | 2,062 |
| Deferred income taxes | 11,895 | 12,590 |
| Prepaid expenses and other assets | 17,694 | 14,253 |
| **TOTAL CURRENT ASSETS** | 298,852 | 279,783 |
| **PROPERTY, PLANT & EQUIPMENT** | 27,108 | 28,236 |
| **GOODWILL** | 29,840 | 29,840 |
| **PURCHASED INTANGIBLE ASSETS** | 21,346 | 23,651 |
| **NET INVESTMENT IN SALES-LEASES**, net of allowances of $1,756 in 2006 and $1,926 in 2005 | 35,469 | 34,758 |
| **TOTAL ASSETS** | $412,615 | $396,268 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| **CURRENT LIABILITIES** | | |
| Accounts payable | $ 30,492 | $ 29,879 |
| Other current liabilities | 58,673 | 54,386 |
| **TOTAL CURRENT LIABILITIES** | 89,165 | 84,265 |
| **DEFERRED TAX LIABILITY** | 69,191 | 70,439 |
| **LEASE RECOURSE LIABILITY** | 14,095 | 14,199 |
| **OTHER LIABILITIES** | 7,109 | 7,034 |
| **SHAREHOLDERS' EQUITY** | | |
| Common stock, $0.001 par value-authorized 100,000,000 shares; issued—27,161,823 shares; outstanding—26,621,991 at June 30, 2006 and 26,264,458 shares at December 31, 2005 | 27 | 27 |
| Additional Paid-In Capital | 123,686 | 120,462 |
| Retained earnings | 116,940 | 114,653 |
| Accumulated other comprehensive income | 1,354 | (36) |
| | 242,007 | 235,106 |
| Less: Treasury stock at cost — 539,832 shares at June 30, 2006 and 897,365 shares at December 31, 2005 | (8,952) | (14,775) |
| **TOTAL SHAREHOLDERS' EQUITY** | 233,055 | 220,331 |
| **TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY** | $412,615 | $396,268 |

See accompanying notes.

**INTER-TEL (DELAWARE), INCORPORATED AND SUBSIDIARIES**
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)**

| (In thousands, except per share amounts) | Three Months Ended June 30, 2006 | Three Months Ended June 30, 2005 | Six Months Ended June 30, 2006 | Six Months Ended June 30, 2005 |
|---|---|---|---|---|
| **NET SALES** | | | | |
| Telecommunications systems, software and related | $100,921 | $101,647 | $193,164 | $194,306 |
| Resale of local, long distance and network services | 15,004 | 13,618 | 29,684 | 26,577 |
| **TOTAL NET SALES** | 115,925 | 115,265 | 222,848 | 220,883 |
| **COST OF SALES** | | | | |
| Telecommunications systems, software and related | 49,628 | 46,904 | 94,111 | 90,301 |
| Resale of local, long distance and network services | 9,535 | 8,316 | 18,697 | 16,572 |
| **TOTAL COST OF SALES** | 59,163 | 55,220 | 112,808 | 106,873 |
| **GROSS PROFIT** | 56,762 | 60,045 | 110,040 | 114,010 |
| Research and development | 8,799 | 8,713 | 17,106 | 17,168 |
| Selling, general and administrative | 40,179 | 40,252 | 78,711 | 78,975 |
| Amortization of purchased intangible assets | 1,185 | 1,122 | 2,316 | 1,884 |
| Write-off of in-process research and development costs | — | — | — | 2,600 |
| Legal judgment and settlement | — | — | 1,300 | — |
| | 50,163 | 50,087 | 99,433 | 100,627 |
| **OPERATING INCOME** | 6,599 | 9,958 | 10,607 | 13,383 |
| Interest and other income | 1,542 | 921 | 2,822 | 1,867 |
| Foreign currency transaction (losses) gains | (358) | 88 | (362) | 141 |
| Interest expense | (14) | (23) | (35) | (46) |
| **INCOME BEFORE INCOME TAXES** | 7,769 | 10,944 | 13,032 | 15,345 |
| **INCOME TAXES** | 2,984 | 4,003 | 5,045 | 6,446 |
| **NET INCOME** | $ 4,785 | $ 6,941 | $ 7,987 | $ 8,899 |
| **NET INCOME PER SHARE — BASIC** | $ 0.18 | $ 0.26 | $ 0.30 | $ 0.34 |
| **NET INCOME PER SHARE — DILUTED** | $ 0.18 | $ 0.26 | $ 0.29 | $ 0.32 |
| **DIVIDENDS PER SHARE** | $ 0.08 | $ 0.08 | $ 0.16 | $ 1.16 |
| Average number of common shares outstanding — Basic | 26,534 | 26,301 | 26,421 | 26,337 |
| Average number of common shares outstanding — Diluted | 27,227 | 27,069 | 27,103 | 27,429 |

See accompanying notes.

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## INTER-TEL (DELAWARE), INCORPORATED AND SUBSIDIARIES
## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

| (In thousands) | Six Months Ended June 30, 2006 | 2005 |
|---|---|---|
| **OPERATING ACTIVITIES** | | |
| Net income | $ 7,987 | $ 8,899 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation of fixed assets | 4,496 | 4,723 |
| Amortization of patents included in R&D expenses | 9 | 111 |
| Amortization of purchased intangible assets | 2,316 | 1,884 |
| Purchased in-process research and development | — | 2,600 |
| Provision for losses on receivables | 323 | 846 |
| Provision for losses on leases | 1,389 | 1,814 |
| Provision for inventory valuation | 653 | 256 |
| Share based compensation expense | 2,135 | — |
| Excess tax benefits from stock options exercised | (1,090) | — |
| Decrease in other liabilities | (1,146) | (442) |
| (Gain) / Loss on sale of property and equipment | (9) | 22 |
| Deferred income taxes | (555) | (129) |
| Changes in operating assets and liabilities | (3,295) | (8,518) |
| **NET CASH PROVIDED BY OPERATING ACTIVITIES** | 13,213 | 12,066 |
| **INVESTING ACTIVITIES** | | |
| Purchases of available for sale short-term investments | (38,762) | (21,387) |
| Maturities and sales of available for sale investments | 38,570 | 21,132 |
| Additions to property, plant and equipment | (3,391) | (4,279) |
| Proceeds from disposal of property, plant and equipment | 31 | 16 |
| Cash used in acquisitions | (9) | (27,765) |
| **NET CASH USED IN INVESTING ACTIVITIES** | (3,561) | (32,283) |
| **FINANCING ACTIVITIES** | | |
| Cash dividends paid | (4,212) | (30,673) |
| Treasury stock purchases | — | (13,777) |
| Payments on term debt | (24) | (23) |
| Proceeds from stock issued under the Employee Stock Purchase Plan | 542 | 582 |
| Proceeds from exercise of stock options | 3,820 | 6,320 |
| Excess tax benefits from stock options exercised | 1,090 | — |
| **NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES** | 1,216 | (37,571) |
| **EFFECT OF EXCHANGE RATE CHANGES** | 1,390 | (524) |
| **INCREASE (DECREASE) IN CASH AND EQUIVALENTS** | 12,258 | (58,312) |
| **CASH AND EQUIVALENTS AT BEGINNING OF PERIOD** | 103,774 | 152,330 |
| **CASH AND EQUIVALENTS AT END OF PERIOD** | $116,032 | $ 94,018 |

See accompanying notes.

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**INTER-TEL (DELAWARE), INCORPORATED AND SUBSIDIARIES**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**
June 30, 2006

## NOTE A—BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles applicable to interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the results for the interim periods presented have been included. Operating results for the quarter and six months ending June 30, 2006 are not necessarily indicative of the results that may be expected for the year ended December 31, 2006. The balance sheet at December 31, 2005 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. For further information, refer to the consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2005.

During the three month period ended June 30, 2006, Inter-Tel, Incorporated completed a reincorporation as a Delaware corporation and changed its name to Inter-Tel (Delaware), Incorporated ("Inter-Tel"). In connection with this change, the Company's common stock was changed from a no-par value stock to a $0.001 par value stock. All prior periods included in these financial statements include a reclassification between common stock and additional paid-in-capital to conform to the June 30, 2006 classification.

Certain other prior period amounts have been reclassified to conform with the current period presentation.

### Share-Based Payments

In December 2004, the Financial Accounting Standards Board ("FASB") revised Statement of Financial Accounting Standards No. 123 ("SFAS No. 123R"), "Share-Based Payment," which establishes accounting for share-based awards exchanged for employee services and requires companies to expense the estimated fair value of these awards over the requisite employee service period. On April 14, 2005, the U.S. Securities and Exchange Commission adopted a new rule amending the effective dates for SFAS 123R. In accordance with the new rule, the accounting provisions of SFAS No. 123R were effective for the Company beginning January 1, 2006.

Under SFAS 123R, share-based compensation cost is measured at the grant date, based on the estimated fair value of the award, and is recognized as expense over the employee's requisite service period. As of January 1, 2006 the Company had no unvested awards with market or performance conditions. As further described in Note F to the Condensed Consolidated Financial Statements, the Company granted performance based shares during the three-month period ended June 30, 2006. No expense has been recorded for the performance shares as vesting is not considered probable. The Company adopted the provisions of SFAS No. 123R on January 1, 2006, the first day of the Company's fiscal year 2006, using a modified prospective application, which provides for certain changes to the method for recognizing share-based compensation. Under the modified prospective application, prior periods are not revised for comparative purposes. The provisions of SFAS No. 123R apply to new awards and to awards that were outstanding with future service periods on the effective date. Estimated compensation expense for awards outstanding with future service periods at the effective date will be recognized over the remaining service period using the compensation cost previously calculated for pro forma disclosure purposes under FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123").

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**Contingencies**

We are a party to various claims and litigation in the normal course of business. Management's current estimated range of liability related to various claims and pending litigation is based on claims for which our management can estimate the amount and range of loss. Because of the uncertainties related to both the amount and range of loss on the remaining pending claims and litigation, management is unable to make a reasonable estimate of the liability that could result from an unfavorable outcome. As additional information becomes available, we will assess the potential liability related to our pending litigation and revise our estimates. Such revisions in our estimates of the potential liability could materially impact our results of operations and financial position. However, at June 30, 2006, management did not believe the ultimate impact of various claims and pending litigation would have a material adverse impact on the results of operations, liquidity or financial condition of the Company.

As disclosed and accrued in 2005, a Florida state court jury rendered a verdict against Inter-Tel ("the Florida trial") with respect to a certain commercial dispute with a prior Executone dealer, in the net amount of approximately $7.4 million. Although the Company is appealing the verdict, the Company has accrued the net verdict amount, plus related legal costs incurred. Should the Company be successful or unsuccessful in the appeals process, these costs may be adjusted in the future. In connection with the appeal of the Florida trial, the Company posted collateral of $6.3 million in order to secure an appellate bond. In March 2006, other prior Executone dealers filed a complaint in Columbus, Ohio similar to the complaint in the Florida trial. The Company is in the process of evaluating the complaint and conducting initial discovery.

In the quarter ended March 31, 2006, the Company settled another legal matter in connection with a longstanding dispute with a former international dealer that existed as of December 31, 2005. The Company recorded an accrual for the settlement amount and related fourth quarter legal fees as of December 31, 2005. The settlement plus related fourth quarter legal fees totaled $1.6 million. Additional legal fees totaling approximately $1.3 million were recorded as period costs during the first quarter of 2006 relating to this matter.

On January 5, 2005, the Company received court approval of a civil settlement agreement (the "Civil Settlement") and a criminal plea agreement (the "Plea Agreement") with the United States of America, each dated as of December 8, 2004 and disclosed on that same date. The court approval of the Civil Settlement and Plea Agreement resolved the investigation of the Department of Justice into the participation of Inter-Tel Technologies, Inc., the Company's wholly-owned subsidiary ("Technologies"), in a federally administered "E-Rate program" to connect schools and libraries to the Internet. In connection with the Civil Settlement, Technologies paid a penalty of $6.7 million and forgave the collection of certain accounts receivable of $0.3 million related to Technologies' participation in the E-Rate program. In connection with the Plea Agreement, Technologies entered guilty pleas to charges of mail fraud and an antitrust violation. Under the Plea Agreement, Technologies paid a fine of $1.7 million and is observing a three-year probationary period, which has, among other things, required Technologies to implement a comprehensive corporate compliance program. On December 20, 2005, in connection with the Civil Settlement, Technologies paid outside counsel for the plaintiffs in that action $0.1 million in settlement of their demand for attorney's fees and costs. On March 10, 2006, Technologies agreed to pay an additional $0.4 million to plaintiffs' inside counsel in settlement of their separate demand for fees and costs.

Inter-Tel recorded approximately $9.5 million in costs through 2005, including criminal fines, civil settlement and restitution, uncompensated E-Rate work, accounts receivable forgiveness, and related attorneys' fees and other expenses. The payments constituting the primary components of the settlement are not tax deductible. The effect of the resolution was recorded in 2004, although the Company has continued to incur additional legal expenses in connection with the defense of a former employee in connection with this matter pursuant to California statute.

In addition, on January 21, 2005, Inter-Tel Technologies received notification from the Federal Communications Commission that the Technologies subsidiary was temporarily suspended from participation in the E-Rate program pending a final hearing to determine a possible debarment of three (3) years or more. Technologies contested the scope and length of the proposed debarment from the E-Rate program. The Company was notified on June 30, 2006 that on or about June 21, 2006, the FCC issued its

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final decision on the matter and imposed upon Technologies a debarment from the E-Rate program of one (1) year from June 30, 2006. Reasons for the shorter period were, among other factors, that Technologies had instituted a compliance program and been cooperative in the investigation and ongoing hearings with the Department of Justice. The FCC order further clarified that the parent and other subsidiaries were not debarred. The Company recorded no revenues since January 21, 2005 relating to Technologies' participation in the E-Rate program.

During the second quarter of 2005, we identified variances in our sales processes as they relate to certain terms included in the U.S. General Services Administration (GSA) pricing and trade agreement requirements applicable to our business. As a result of this identification, Inter-Tel made voluntary self-disclosure of the matter to the Inspector General of the GSA. The potential variances relate primarily to noncompliance with certain pricing thresholds and noncompliance with trade agreements that are applicable to transactions with certain government agencies. We continue to monitor our compliance and have taken appropriate corrective measures with respect to these potential variances. In the second quarter of 2005, we accrued $1.8 million in estimated pre-tax adjustments, including reductions in net sales and increases to costs, fines and penalties that may be incurred to correct this issue, of which we have paid $1.2 million through June 30, 2006. Our estimate at June 30, 2006 remains the same as the total identified as of the end of the second quarter of 2005. The total sales potentially subject to the GSA agreements were approximately $5.5 million during the period from March 28, 2001 through June 10, 2005. Our current contract with the GSA expires in August 2006, and we have requested and expect to receive an extension of that contract.

On June 16, 2006, a shareholder class action suit was brought against Inter-Tel and selected Board members in Delaware state court. On June 16 and June 20, 2006, respectively, two additional shareholder class actions against the Company and each of its Board members were filed in Arizona state court. The Delaware action, as amended July 14, 2006, raises claims related to the reincorporation filing by Inter-Tel in Delaware and primarily seeks injunctive relief. The Arizona actions claim breach of fiduciary duty related to the 13D filings by the Company's former CEO. The Company is in the process of evaluating these class action suits.

### Inventories

We value our inventories at the lower of cost (principally on a standard cost basis, which approximates the first-in, first-out (FIFO) method) or market.

### Recent Accounting Pronouncements

In June 2006, the FASB ratified Emerging Issues Task Force (EITF) Issue No. 06-3, "*How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross Versus Net Presentation).*" This standard allows companies to present in their statements of income any taxes assessed by a governmental authority that are directly imposed on revenue-producing transactions between a seller and a customer, such as sales, use, value-added, and some excise taxes, on either a gross (included in revenue and costs) or a net (excluded from revenue) basis. This standard will be effective for us in interim periods and fiscal years beginning after December 15, 2006. We are currently evaluating the potential impact of this issue on our financial position and results of operations, but do not believe the impact of the adoption of this standard will be material.

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation Number 48 (FIN 48), "Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109." The interpretation contains a two step approach to recognizing and measuring uncertain tax positions accounted for in accordance with SFAS No. 109. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount which is more than 50% likely of being realized upon ultimate settlement. The provisions are effective for the company beginning in the first quarter of 2007. The company is evaluating the impact this statement will have on its consolidated financial statements.

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## NOTE B—EARNINGS PER SHARE

Diluted earnings per share assume that outstanding common shares were increased by shares issuable upon the exercise of all outstanding stock options for which the market price exceeds exercise price, less shares which could have been purchased with related proceeds, if the effect would not be antidilutive.

The following table sets forth the computation of basic and diluted earnings per share:

| (In thousands, except per share amounts) | Three Months Ended June 30, 2006 | Three Months Ended June 30, 2005 | Six Months Ended June 30, 2006 | Six Months Ended June 30, 2005 |
|---|---|---|---|---|
| Numerator: Net income | $ 4,785 | $ 6,941 | $ 7,987 | $ 8,899 |
| Denominator: | | | | |
| Denominator for basic earnings per share — weighted average shares | 26,534 | 26,301 | 26,421 | 26,337 |
| Effect of dilutive securities: | | | | |
| Employee and director stock options | 693 | 768 | 682 | 1,092 |
| Denominator for diluted earnings per share — adjusted weighted average shares and assumed conversions | 27,227 | 27,069 | 27,103 | 27,429 |
| Basic earnings per share | $ 0.18 | $ 0.26 | $ 0.30 | $ 0.34 |
| Diluted earnings per share | $ 0.18 | $ 0.26 | $ 0.29 | $ 0.32 |
| Options excluded from diluted net earnings per share calculations (1) | 1,120 | 669 | 1,120 | 252 |

(1) At June 30, 2006 and 2005, options to purchase shares of Inter-Tel stock were excluded from the calculation of diluted net earnings per share because the exercise price of these options was greater than the average market price of the common shares for the respective periods, and therefore the effect would have been antidilutive.

(2) The adoption of FAS123R, effective January 1, 2006 also changed the method of computation of dilutive shares for 2006. If the same method used to determine dilutive shares in 2005 was used in 2006, the dilutive shares would have been 769 and 772 for the three month and six month periods ended June 30, 2006. This did not change the diluted earnings per share for the three month or six month periods ended June 30, 2006.

## NOTE C — ACQUISITIONS

**Lake.** On February 28, 2005, Inter-Tel Lake Ltd., a wholly owned Irish subsidiary of Inter-Tel, executed an agreement for the purchase of 100% of the issued share capital of Lake Communications Limited and certain affiliated entities (collectively, "Lake") for $28.7 million (including capitalized transaction costs of $0.7 million), plus an earn-out of up to $17.6 million based upon certain targets relating to operating results for Lake through the first eighteen months following the closing date of the transaction. The transaction closed out of escrow on March 4, 2005 upon the release from escrow of closing documentation. In total, the company recorded $19.3 million of intangible assets of which $2.6 million was charged to expense in the first quarter of 2005 as in-process research and development costs with the balance being amortized over eight years. Additionally we recorded $8.7 million of goodwill, which is non-amortizable. As of June 30, 2006, none of the potential earn-out has been accrued, as there is no amount that has been estimated as being probable of being paid. The final measurement for the possible earn-out will occur during the Company's third fiscal quarter of 2006.

Lake, based in Dublin, Ireland, is a provider of converged communications products in the under 40 user market, including EncoreCX® products currently being distributed by Inter-Tel in the United States.

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Lake designs and develops its products for sale through a distribution network of telecom operators and distributors, including Inter-Tel in the United States. Lake outsources its manufacturing to third-party suppliers.

The acquisition discussed above was not a material business acquisition and has been accounted for using the purchase method of accounting. The results of operations of this acquisition have been included in our accompanying consolidated statements of operations from the date of the acquisition.

The weighted-average amortization period for total purchased intangibles as of June 30, 2006 and December 31, 2005 was approximately 7.6 years and 7.5 years for each period, respectively. The weighted-average amortization period as of June 30, 2006 and December 31, 2005 for developed technology was approximately 7.5 and 7.3 years for each period, respectively, and 7.8 years for both periods for customer lists and non-compete agreements.

## NOTE D — SEGMENT INFORMATION

Inter-Tel follows Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" ("SFAS 131"). SFAS 131 established standards for reporting information regarding operating segments in annual financial statements and requires selected information for those segments to be presented in interim financial reports issued to stockholders. SFAS 131 also established standards for related disclosures about products and services and geographic areas. Operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision maker, or decision-making group, in making decisions as to how to allocate resources and assess performance. The Company's chief decision maker, as defined under SFAS 131, is the Chief Executive Officer.

We view our operations as primarily composed of two segments: (1) our principal segment, which includes sales of telephone systems, telecommunications software, hardware and related services ("principal segment"), and (2) network services, including resale of local and long distance calling services, voice circuits and data circuits through NetSolutions®, as well as commissions earned by Network Services Agency, our division serving as an agent selling local and network services such as T-1 access, frame relay and other voice and data circuit services on behalf of Regional Bell Operating Companies (RBOCs) and local exchange carriers (collectively, "Network Services"). Sales of these systems, software, related services and Network Services are provided through the Company's direct sales offices and dealer network to business customers in North America, and in parts of Europe, Australia, South Africa and Asia. As a result, financial information disclosed represents substantially all of the financial information related to the Company's two principal operating segments. Results of operations for the resale of local, long distance and network services segment, if the operations were not included as part of the consolidated group, could differ materially, as the operations are integral to the total telephony solution offered by us to our customers.

As of and for the three and six month periods ended June 30, 2006 and 2005, financial information for the business segments was as follows:

| (In thousands, except per share amounts) | As Of and For The Three Months Ended June 30, 2006 | | |
|---|---|---|---|
| | Principal Segment | Resale of Local, Long Distance and Network Services | Total |
| Net sales | $100,921 | $15,004 | $115,925 |
| Gross profit | 51,293 | 5,469 | 56,762 |
| Operating income | 4,640 | 1,959 | 6,599 |
| Interest and other income | 1,505 | 37 | 1,542 |
| Foreign currency transaction losses | (358) | — | (358) |
| Interest expense | (14) | — | (14) |
| Net income | $ 3,748 | $ 1,037 | $ 4,785 |
| Net income per diluted share (1) | $ 0.14 | $ 0.04 | $ 0.18 |
| Weighted average diluted shares (1) | 27,227 | 27,227 | 27,227 |
| Goodwill | $ 27,705 | $ 2,135 | $ 29,840 |
| Total assets | 398,772 | 13,843 | 412,615 |
| Depreciation and amortization | $ 3,437 | $ 19 | $ 3,456 |

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| (In thousands, except per share amounts) | As Of and For The Three Months Ended June 30, 2005<br>Principal Segment | Resale of Local, Long Distance and Network Services | Total |
|---|---|---|---|
| Net sales | $101,647 | $13,618 | $115,265 |
| Gross profit | 54,743 | 5,302 | 60,045 |
| Operating income | 7,557 | 2,401 | 9,958 |
| Interest and other income | 884 | 37 | 921 |
| Foreign currency transaction gains | 88 | — | 88 |
| Interest expense | (19) | (4) | (23) |
| Net income | $ 5,613 | $ 1,328 | $ 6,941 |
| Net income per diluted share (1) | $ 0.21 | $ 0.05 | $ 0.26 |
| Weighted average diluted shares (1) | 27,069 | 27,069 | 27,069 |
| Goodwill | $ 27,705 | $ 2,135 | $ 29,840 |
| Total assets | 373,722 | 10,269 | 383,991 |
| Depreciation and amortization | $ 3,633 | $ 14 | $ 3,647 |

| (In thousands, except per share amounts) | As Of and For The Six Months Ended June 30, 2006<br>Principal Segment | Resale of Local, Long Distance and Network Services | Total |
|---|---|---|---|
| Net sales | $193,164 | $29,684 | $222,848 |
| Gross profit | 99,053 | 10,987 | 110,040 |
| Operating income | 5,767 | 4,840 | 10,607 |
| Interest and other income | 2,736 | 86 | 2,822 |
| Foreign currency transaction losses | (362) | 0 | (362) |
| Interest expense | (34) | (1) | (35) |
| Net income | $ 5,065 | $ 2,922 | $ 7,987 |
| Net income per diluted share (1) | $ 0.18 | $ 0.11 | $ 0.29 |
| Weighted average diluted shares (1) | 27,103 | 27,103 | 27,103 |
| Goodwill | $ 27,705 | $ 2,135 | $ 29,840 |
| Total assets | 398,772 | 13,843 | 412,615 |
| Depreciation and amortization | $ 6,782 | $ 39 | $ 6,821 |

| (In thousands, except per share amounts) | As Of and For The Six Months Ended June 30, 2005<br>Principal Segment | Resale of Local, Long Distance and Network Services | Total |
|---|---|---|---|
| Net sales | $194,306 | $26,577 | $220,883 |
| Gross profit | 104,005 | 10,005 | 114,010 |
| In-process research and development | 2,600 | — | 2,600 |
| Operating income | 9,016 | 4,367 | 13,383 |
| Interest and other income | 1,789 | 78 | 1,867 |
| Foreign currency transaction gains | 141 | — | 141 |
| Interest expense | (42) | (4) | (46) |
| Net income | $ 6,477 | $ 2422 | $ 8,899 |
| Net income per diluted share (1) | $ 0.24 | $ 0.09 | $ 0.32 |
| Weighted average diluted shares (1) | 27,429 | 27,429 | 27,429 |
| Goodwill | $ 27,705 | $ 2,135 | $ 29,840 |
| Total assets | 373,722 | 10,269 | 383,991 |
| Depreciation and amortization | $ 6,688 | $ 30 | $ 6,718 |

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(1) Options that are antidilutive because the exercise price was greater than the average market price of the common shares are not included in the computation of diluted earnings per share.

As illustrated in the table below, our revenues are generated predominantly in the United States. Total revenues generated from U.S. customers totaled $103.9 million or 89.7% of total revenues and $104.3 million or 90.5% of total revenues for the three months ended June 30, 2006 and 2005, respectively. For the six months ended June 30, 2006 and 2005, revenues generated from US customers totaled $201.6 million or 90.5% of total revenues and $203.9 million or 92.3% of total revenues respectively. Refer to the tables below for additional geographical revenue data.

| | Quarter Ended June 30, 2006 | | Quarter Ended June 30, 2005 | |
|---|---|---|---|---|
| **Source of net sales** | **$** | **%** | **$** | **%** |
| Domestic | $103,941 | 89.7% | $104,279 | 90.5% |
| Lake Communications | 7,242 | 6.2% | 7,907 | 6.8% |
| Other International | 4,742 | 4.1% | 3,079 | 2.7% |
| Total net sales | $115,925 | 100.0% | $115,265 | 100.0% |

| | Six Months Ended June 30, 2006 | | Six Months Ended June 30, 2005 | |
|---|---|---|---|---|
| **Source of net sales** | **$** | **%** | **$** | **%** |
| Domestic | $201,645 | 90.5% | $203,943 | 92.3% |
| Lake Communications | 13,116 | 5.9% | 10,497 | 4.8% |
| Other International | 8,087 | 3.6% | 6,443 | 2.9% |
| Total net sales | $222,848 | 100.0% | $220,883 | 100.0% |

Lake Communications is based in Dublin, Ireland with a majority of its sales made to the United Kingdom, Australia, other European countries, and South Africa. Other International revenues identified in the table above primarily consist of revenues from Inter-Tel's UK operations, including sales from Swan Solutions. Our UK offices sell predominantly into the United Kingdom and other European countries. In the three months ended June 30 of 2006 and 2005, revenues from customers located internationally accounted for 10.3% and 9.5% of total revenues, respectively. In the six months ended June 30, 2006 and 2005, revenues from customers located internationally accounted for 9.5% and 7.7% of total revenues, respectively. Our principal segment generated substantially all of our foreign revenues for 2006 and 2005. For the quarter ended June 30, 2006, $1.6 million of income before income taxes was generated from our foreign operations and $2.0 million for the six months ended June 30, 2006. All sales made between Inter-Tel divisions are eliminated and are not represented in the above amounts or in the Consolidated Statements of Income.

Our applicable long-lived assets at June 30, 2006, included Property, Plant & Equipment; Goodwill; and Purchased Intangible Assets. The net amount located in the United States was $52.3 million and the amount in foreign countries was $26.0 million at June 30, 2006. At December 31, 2005, the net amount located in the United States was $54.4 million and the amount in foreign countries was $27.3 million.

## NOTE E — NET INVESTMENT IN SALES-LEASES

Net investment in sales-leases represents the value of sales-leases presently held under our TotalSolution program. We currently sell the rental payments due to us from most of the sales-leases. We maintain reserves against our estimate of potential credit losses for the balance of sales-leases held and for the balance of sold rental payments remaining unbilled. The following table provides detail on the total net balances in sales-leases:

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| (In thousands) | June 30, 2006 | December 31, 2005 |
|---|---|---|
| Lease balances included in consolidated accounts receivable, net of allowances of $1,189 in 2006, and $980 in 2005 | $ 8,075 | $ 8,860 |
| Net investment in Sales-Leases: | | |
| Current portion, net of allowances of $900 in 2006, and $998 in 2005 | 17,497 | 19,699 |
| Long-term portion, includes residual amounts of $1,103 in 2006 and, $625 in 2005, net of allowances of $1,756 in 2006, and $1,926 in 2005 | 35,469 | 34,758 |
| Total investment in Sales-Leases, net of allowances of $3,845 in 2006, and $3,904 in 2005 | 61,041 | 63,317 |
| Sold rental payments remaining unbilled (subject to limited recourse provisions), net of allowances of $14,095 in 2006, and $14,199 in 2005 | 258,240 | 256,143 |
| Total balance of sales-leases and sold rental payments remaining unbilled, net of allowances | $319,281 | $319,460 |
| Total allowances for entire lease portfolio (including limited recourse liabilities) | $ 17,940 | $ 18,103 |

Reserve levels are established based on portfolio size, loss experience, levels of past due accounts and periodic, detailed reviews of the portfolio. Recourse on the sold rental payments is contractually limited to a percentage of the net credit losses in a given annual period as compared to the beginning portfolio balance for a specific portfolio of sold leases. While our recourse is limited, we maintain reserves at a level that we believe are sufficient to cover all anticipated credit losses. The aggregate reserve for uncollectible lease payments and recourse liability represents the reserve for the entire lease portfolio.

These reserves are either netted against consolidated accounts receivable, netted against current or long-term "investment in sales-leases" or included in long-term liabilities for sold rental payments remaining unbilled. Sales of rental payments per period are as follows:

| (In thousands) | Six Months Ended June 30, 2006 | Year Ended December 31, 2005 |
|---|---|---|
| Sales of rental payments | $ 50,719 | $119,060 |
| Sold payments remaining unbilled at end of period | $272,335 | $270,342 |

Sales of rental payments represent the gross selling price or total present value of the payment stream on the sale of the rental payments to third parties. Sold payments remaining unbilled at the end of the period represent the total balance of leases that is not included in our balance sheet. We do not expect to incur any significant losses in excess of reserves from the recourse provisions related to the sale of rental payments.

During 2006, the Company has entered into "rate-lock" agreements with a financial institution in the form of commitments to sell the cash flow streams for leases at a fixed interest rate to the financial institution. As of June 30, 2006, the Company has one outstanding agreement in place to sell cash flow streams with a present value of $15.0 million in December 2006 at a fixed interest rate to a financial institution. As part of the agreement, the Company has the option to pay $300,000 to the financial institution to cancel the commitment. Subsequent to June 30, 2006, the Company entered into another agreement to sell cash flow streams with a present value of $10.0 million in March 2007 at a fixed interest rate to a financial institution. As part of the agreement, the Company has the option to pay $100,000 to the financial institution to cancel the commitment.

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## NOTE F — SHARE BASED COMPENSATION

At June 30, 2006, the Company had five active share-based employee compensation plans, including an Employee Stock Purchase Plan. Stock option awards granted from these plans are granted at the fair market value on the date of grant, and vest over a period determined at the time the options are granted, ranging from six months to five years, and generally have a maximum term of ten years. Certain options provide for accelerated vesting if there is a change in control (as defined in the plans). When options are exercised, treasury shares of the Company's common stock are re-issued. Prior to December 31, 2005, the Company accounted for share-based employee compensation, including stock options, using the method prescribed in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related Interpretations ("APB Opinion No. 25"). Under APB Opinion No. 25, stock options are granted at market price and no compensation cost is recognized, and a disclosure is made regarding the pro forma effect on net earnings assuming compensation cost had been recognized in accordance with Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"). During December 2004, the FASB issued SFAS No. 123R, which requires companies to measure and recognize compensation expense for all share-based payments at fair value. SFAS No. 123R eliminates the ability to account for share-based compensation transactions using APB Opinion No. 25, and generally requires that such transactions be accounted for using prescribed fair-value-based methods. SFAS No. 123R permitted public companies to adopt its requirements using one of two methods: (a) a "modified prospective" method in which compensation costs are recognized beginning with the effective date based on the requirements of SFAS No. 123R for all share-based payments granted or modified after the effective date, and based on the requirements of SFAS No. 123 for all awards granted to employees prior to the effective date of SFAS No. 123R that remain unvested on the effective date or (b) a "modified retrospective" method which includes the requirements of the modified prospective method described above, but also permits companies to restate based on the amounts previously recognized under SFAS No. 123 for purposes of pro forma disclosures either for all periods presented or prior interim periods of the year of adoption. Effective January 1, 2006, the Company adopted SFAS No. 123R using the modified prospective method. No share-based employee compensation cost has been reflected in net income prior to the adoption of SFAS No. 123R. Results for prior periods have not been restated.

The adoption of SFAS No. 123R reduced income before income tax expense for the three and six months ended June 30, 2006 by approximately $1.1 million and $2.1 million respectively and reduced net income for the three and six months ended June 30, 2006 by approximately $0.9 million and $1.7 respectively. Basic and diluted net income per common share for the three and six months ended June 30, 2006 are lower by $0.03 and $0.06, respectively, than if the Company had continued to follow APB Opinion No. 25. The total value of the stock options awards is expensed ratably over the service period of the employees receiving the awards. As of June 30, 2006, total unrecognized compensation cost related to stock option awards was approximately $7.7 million and the related weighted-average period over which it is expected to be recognized is approximately 2.5 years.

Total estimated share-based compensation expense, related to all of the Company's share-based awards, recognized for the three and six months ended June 30, 2006 was comprised as follows (in thousands, except per share data):

| | Three Months Ended June 30, 2006 | Six Months Ended June 30, 2006 |
|---|---|---|
| Cost of Revenues | $ 50 | $ 123 |
| Research and development | 282 | 571 |
| Selling, General and Administrative | 752 | 1,441 |
| Share-based compensation expense before income taxes | 1,084 | 2,135 |
| Related income tax benefits | 198 | 447 |
| Share-based compensation expense, net of taxes | $ 886 | $1,688 |
| Net share-based compensation expense, per common share: | | |
| Basic | $ 0.03 | $ 0.06 |

| | | |
|---|---|---|
| Diluted | $ 0.03 | $ 0.06 |

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Prior to the adoption of SFAS No. 123R, the Company presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the condensed consolidated statements of cash flows. SFAS No. 123R requires the cash flows resulting from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. The $1.1 million excess tax benefit classified as a financing cash inflow in the Company's accompanying condensed consolidated statements of cash flows for the six months ended June 30, 2006 respectively, would have been classified as an operating cash inflow if the Company had not adopted SFAS No. 123R.

A summary of stock options activity within the Company's share-based compensation plans and changes for the six months ended June 30, 2006 is as follows:

| | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (years) | Aggregate Intrinsic Value |
|---|---|---|---|---|
| Balance at December 31, 2005 | 3,855,988 | $16.36 | | |
| Granted | 616,750 | $23.17 | | |
| Exercised | (326,573) | $11.85 | | |
| Terminated/expired | (103,127) | $19.89 | | |
| Balance at June 30, 2006 | 4,043,038 | $17.66 | 6.4 | $13,746,329 |
| Exercisable at June 30, 2006 | 2,709,081 | $16.65 | 5.5 | $11,947,047 |

The intrinsic value of options exercised during the six months ended June 30, 2006 was $3,089,000.

The fair value of each stock option award is estimated on the date of the grant using the Black-Scholes option pricing model with the following assumptions:

| | Six Months Ended June 30, 2006 | Six Months Ended June 30, 2005 |
|---|---|---|
| Expected dividend yield | 1.37%-1.53% | 1.52% |
| Expected stock price volatility | 0.41-0.53 | 0.48-0.58 |
| Risk-free interest rate | 4.76%-4.98% | 3.77% |
| Expected life of options | 3-5 Years | 3-5 years |

The expected dividend yield is based on expected annual dividend to be paid by the Company as a percentage of the market value of the Company's stock as of the date of grant. The Company determined volatility using historical volatility. The risk-free interest rate is based on the U.S. treasury security rate in effect as of the date of grant. The expected lives of options are based on historical data of the Company, adjusted for expected future activity. The weighted average fair value of stock options granted during the six months ended June 30, 2006 and June 30, 2005 was $8.49 and $6.34, respectively.

The following table illustrates the effect on net income and net income per common share as if the Company had applied the fair value recognition provisions of SFAS No. 123 to all outstanding stock option awards for periods presented prior to the Company's adoption of SFAS No. 123R (amounts in thousands, except per share amounts):

| | | THREE MONTHS ENDED JUNE 30, 2005 |
|---|---|---|
| Net income, as reported | $ | 6,941 |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects (1) | | (6,518) |
| Pro-forma net income | $ | 423 |
| Net income per common share: | | |
| Basic, as reported | $ | 0.26 |
| Basic, pro forma | $ | 0.02 |
| Diluted, as reported | $ | 0.26 |
| Diluted, pro forma | $ | 0.02 |

| | | SIX MONTHS ENDED JUNE 30, 2005 |
|---|---|---|
| Net income, as reported | $ | 8,899 |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects (1) | | (7,243) |
| Pro-forma net income | $ | 1,656 |
| Net income per common share: | | |
| Basic, as reported | $ | 0.34 |
| Basic, pro forma | $ | 0.06 |
| Diluted, as reported | $ | 0.32 |
| Diluted, pro forma | $ | 0.06 |

(1) On April 26, 2005, the Compensation Committee of the Board of Directors of Inter-Tel, with the approval of the board of directors, approved the acceleration of the vesting of certain unvested stock options previously granted to employees under the Company's 1994 Long Term Incentive Plan, 1997 Long Term Incentive Plan and the Acquisition Stock Option Plan. With the exception of any options granted to all Directors and Named Executive Officers, all unvested options with exercise prices greater than the closing price as of the close of the Nasdaq stock market on May 3, 2005 ($19.13) became exercisable in full. Such options would otherwise have vested from time to time over the next five years. Approximately 617,000 options were accelerated at grant prices ranging from $19.16 to $31.58. All other terms and conditions applicable to outstanding stock option grants, including the exercise prices and number of shares subject to the accelerated options, were unchanged. This acceleration of the vesting provision increased the stock based compensation expense and decreased the pro forma net income shown in the table above by $5.4 million for the three months and six months ended June 30, 2005.

**Employee Stock Purchase Plan**

Under the Employee Stock Purchase Plan (the "Purchase Plan"), employees are granted the right to purchase shares of Common Stock at a price per share that is 85% of the lesser of the fair market value of the shares at: (i) the participant's entry date into each six-month offering period, or (ii) the end of each six-month offering period. Employees may designate up to 10% of their compensation for the purchase of stock. Included in the share based compensation expense for the three and six months ended June 30, 2006 is $36,000 and $97,000 respectively for the expense related to the Purchase Plan.

**Performance Shares**

During the three months ended June 30, 2006, the Company granted 41,000 performance shares. The performance share awards by their terms vest primarily in connection with the achievement by the Company of certain earnings per share targets over the Company's fiscal years ended December 31, 2007 and December 31, 2008, with 50% vesting each year (on April 27 following the close of each

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respective fiscal year) upon the achievement of such targets. In the event either target is missed, the applicable shares for that year do not vest and are forfeited. The market price of the Company's common stock on the date of grant was $23.44. As of June 30, 2006, no compensation expense has been recorded for these awards, as it is not yet probable that the performance targets will be met.

### NOTE G — SUBSEQUENT EVENT

*Acquisition Offer.* On July 28, 2006, as noted in Steve G. Mihaylo's Form 13D filing, Mr. Mihaylo and Vector Capital Corporation submitted an unsolicited offer to acquire all shares of Inter-Tel Common Stock, except for those shares owned by Mr. Mihaylo, for $22.50 per share, subject to the negotiation of an agreement and other factors. Pursuant to a Settlement Agreement entered into between the Company and Mr. Mihaylo on May 5, 2006, and amended on June 28, 2006, Inter-Tel's Board of Directors has until August 11, 2006 to respond to the offer.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. For further information regarding forward-looking statements, see "Forward Looking Statements" in Item 1A, Risk Factors.

### Overview

Inter-Tel (Delaware), Incorporated (Nasdaq: INTL) ("Inter-Tel"), originally incorporated in Arizona in 1969 and reincorporated into Delaware in 2006, is a single point of contact, full service provider of converged voice and data business communications systems, voice mail systems and networking applications. Our customers include business enterprises, federal, state and local government agencies and non-profit organizations. We market and sell the following products and services:

- Inter-Tel Axxess® and Inter-Tel 5000 Network Communications Solutions converged voice and data business communication systems,
- Lake Communications converged voice and data business communication systems, including those sold in the US under the EncoreCX® brand,
- integrated voice mail, voice processing and unified messaging systems,
- managed services, including voice and data network design, traffic provisioning, and financial solutions packages (leasing),
- networking applications, including the design and implementation of voice and data networks,
- local and long distance calling services, voice circuits, data circuits and other communications services and peripheral products,
- call accounting software, computer-telephone integration (CTI) applications, and
- maintenance and support services for our products.

We have developed a distribution network of direct sales offices, dealers and value added resellers (VARs), which sell our products to organizations throughout the United States and internationally, primarily targeting small-to-medium enterprises, service organizations and governmental agencies. As of June 30, 2006, we had fifty-nine (59) direct sales offices in the United States and a network of hundreds of dealers and VARs, primarily in the United States, that purchase directly from us. Included in our sales office in Phoenix is the primary location for our national and government accounts division, as well as our local, long distance and network services divisions. Our wholesale distribution center is located in Tempe,

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Arizona, which is the primary location from which we distribute products to our network of direct sales offices, dealers and VARs in North America. In addition, we maintain a wholesale distribution office in the United Kingdom that supplies Inter-Tel's dealers and distributors throughout the UK and other parts of Europe, and we have dealers in South Africa and Japan. Our primary research and development facility is located in Chandler, Arizona. In addition, we maintain research and development and software sales offices in Tucson, Arizona, Frederick, Maryland, Washington DC, and in the United Kingdom. As a result of the closing of the Lake acquisition identified below, we also maintain a research and development, and wholesale distribution office in Dublin, Ireland that supplies Inter-Tel's dealers and distributors in the UK, Ireland, other parts of Europe and Australia.

On February 28, 2005, Inter-Tel Lake Ltd., a wholly owned Irish subsidiary of Inter-Tel executed an agreement for the purchase of 100% of the issued share capital of Lake Communications Limited and certain affiliated entities (collectively, "Lake") for $28.7 million (including capitalized transaction costs of $0.7 million), plus an earn-out of up to $17.6 million based upon certain targets relating to operating results for Lake through the first eighteen months following the closing date of the transaction. The transaction closed out of escrow on March 4, 2005 upon the release from escrow of closing documentation. Lake, based in Dublin, Ireland, is a provider of converged communications products in the under 40-user market, including EncoreCX® products distributed by Inter-Tel in the United States. Lake designs and develops its products for sale through a distribution network of telecom operators and distributors, including Inter-Tel in the United States. Lake outsources its manufacturing to third-party suppliers. Lake maintains a research and development and wholesale distribution office in Dublin, Ireland that supplies Inter-Tel's dealers and distributors in the UK, Ireland, South Africa, as well as other parts of Europe and Australia.

Key performance indicators that we use in order to manage our business and evaluate our financial and operating performance include revenues, costs and gross margins, and cash flows.

Inter-Tel recognizes revenue from the following significant sources of revenue:

- *End-user sales and sales-type leases through our direct sales offices and national, government and education accounts division.* We recognize revenue from sales of systems and services to end-user customers upon installation of the systems and performance of the services, respectively, allowing for use by our customers of these systems. We defer pre-payments for communications services and recognize these pre-payments as revenue as the communications services are provided. For our sales-type lease accounting, we record the discounted present values of minimum rental payments under sales-type leases as sales, net of provisions for continuing administration and other expenses over the lease period. We record the lease sales at the time of system sale and installation as discussed above for sales to end user customers, and upon receipt of the executed lease documents. The net rental streams are sold to funding sources on a regular basis with the income streams discounted by prevailing like-term rates at the time of sale. Gains or losses resulting from the sale of net rental payments from such leases are also recorded as net sales.
- *Dealer and VAR sales.* For shipments to dealers and other distributors, our revenue is recognized as products are shipped to the dealers and VARs and services are rendered, because the sales process is complete. Title to these products passes when goods are shipped (free-on-board shipping point). However, in connection with our Lake acquisition, shipments to one international dealer are initially held by that dealer on a consignment basis. Such inventory is owned by Inter-Tel and reported on Inter-Tel's books and records until the inventory is sold to third parties, at which time the revenue is recorded.
- *Resale of long distance.* We recognize revenue from long distance resale services as services are provided.
- *Software Sales.* We recognize revenues from sales of software, such as our new Linktivity products discussed above upon shipment to dealers or end-users.
- *Maintenance and software support.* Maintenance and software support revenue is recognized ratably over the term of the maintenance or support agreement.

*Costs and gross margins.* Our costs of products sold primarily consist of materials, labor and overhead. Our costs of services performed consist primarily of labor, materials and service overhead.

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Total costs of goods and services sold increased 7.1%, or $3.9 million, to $59.2 million for the quarter ended June 30, 2006, compared to $55.2 million for the corresponding period in 2005. Our consolidated gross margin percentage was 49.0% in the second quarter of 2006 compared to 52.1% in the second quarter of 2005. Cost of goods sold was impacted only slightly in the second quarter of 2006 due to FAS 123R related costs associated with expensing of the value of stock options and employee stock purchase plan shares. The increase in the dollar amount of the cost of goods sold was attributable to the higher volume of net sales from our local, long distance and network services divisions, national, government and education accounts divisions, DataNet and international operations, and product transition to our new 5000 series products resulting in higher equipment costs. However, the decrease in gross margin in 2006 compared to 2005 was also attributable to increased competitive and pricing pressures and limited product discounts. In addition, the gross margin percentage was affected by the mix of products sold with a higher proportion of net sales recognized in the divisions identified above, which typically generate lower gross margins than our other divisions within our operating principal segment. Sales through our dealer channel were relatively flat during the three and six months ended June 30, 2006, compared to comparable periods in 2005. Other factors affecting both the increases in costs of goods sold and reductions in overall gross margin percentage are described in greater detail in "Results of Operations" below.

Sales of systems through our direct sales organization typically generate higher gross margins than sales through our dealers and VARs, primarily because we recognize both the wholesale and retail margins on these sales. Conversely, sales of systems through our dealers and VARs typically generate lower gross margins than sales through our direct sales organization, although direct sales typically require higher levels of selling, general and administrative expenses. In addition, our long distance services and Datanet products typically generate lower gross margins than sales of software and system products. For revenues recognized under sales-leases, we record the costs of systems installed as costs of sales. Our margins may vary from period to period depending upon the representation of various distribution channels, products and software as relative percentages of our total sales. In the event that sales through our direct sales offices increase as a percentage of net sales, our overall gross margin could improve. Conversely, in the event net sales to dealers or sales of long distance services increase as a percentage of net sales, our overall gross margin could decline.

Additionally, our operating results depend upon a variety of factors, including the volume and timing of orders received during a period, general economic conditions and world events impacting businesses, patterns of capital spending by customers, the timing of new product announcements and releases by us and our competitors, pricing pressures, the cost and impact of acquisitions and the availability and cost of products and components from our suppliers. Historically, a substantial portion of our net sales in a given quarter has been recorded in the third month of the quarter, with a concentration of such net sales in the last two weeks of the quarter. There are several factors that attribute to this pattern, including the following:

- Customer leases generally expire at end of the month and commence at the beginning of the month, which naturally leads to end-of-period sales. These factors apply to both end-user and dealer sales.
- Internal sales compensation programs for our sales personnel are linked to revenues and the sales commissions generally increase at accelerated rates as sales volumes increase. Sales performance bonuses are also frequently tied to quarter-end and year-end performance targets, providing incentives to sales personnel to close business before the end of each quarter.
- Historically, some price discounting to our dealer channel occurred during the last month of a quarter or year, and some dealers have purchased consistently to take advantage of potential pricing discounts or end-of-quarter promotions. However, such promotions are subject to change at any time, and discounts have been reduced in recent periods in an effort to minimize this trend. Dealer buying habits have been consistent for years.

In addition, we are subject to seasonal variations in our operating results, as net sales for the first and third quarters are frequently less than those experienced during the fourth and second quarters, respectively. Net sales from the second quarter of 2006 followed this historical pattern, as sales increased compared to the first quarter of 2006, and we do not anticipate a significant change in the historical trend.

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*Cash Flows.* At June 30, 2006, Inter-Tel's cash and short-term investments totaled $179.9 million. We also maintain a $10 million unsecured, revolving line of credit with JPMorgan Chase Bank N.A., which is available through June 30, 2007 and ordinarily used to support international letters of credit to suppliers, if necessary. Historically, our primary source of cash has come from net income plus non-cash charges for depreciation and amortization expenses. We have generated cash from continuing operations in every year since 1986. In 1993, 1995 and 1997, the Company received net proceeds from stock offerings, offset in part by cash expended to repurchase the Company's common stock in these and other periods. In addition, Inter-Tel historically has paid cash for capital expenditures relating to property and equipment or acquisitions. Inter-Tel has also received cash proceeds from the exercise of stock options and our Employee Stock Purchase Plan. We believe our working capital and credit facilities, together with cash generated from operations, will be sufficient to develop and expand our business operations, to finance acquisitions of additional resellers of telephony products and other strategic acquisitions or corporate alliances, to repurchase shares of the Company's common stock pursuant to a Board approved repurchase program of up to $75 million announced in February 2005, and to provide adequate working capital for the foreseeable future.

Our consolidated net sales for the quarters ended June 30, 2006 and 2005 were $115.9 million and $115.3 million, respectively. The 0.5% increase in revenue in the second quarter of 2006 compared to the second quarter of 2005 was due to increased revenues in our international operations; local, long distance resale and network services; national, government and education accounts; and our DataNet division. These increases in net sales were offset in part by lower revenues from our direct sales offices, including lease finance revenues, as well as a slight decrease in our dealer network sales. We released our Inter-Tel 5000 v2.0 software and Inter-Tel 5600 late in the second quarter of 2006. The release of these products late in the second quarter had minimal impact on our revenue for the second quarter of 2006. However, based upon feedback from our direct sales offices, dealers and end users, we expect a greater impact on sales from these products for the remainder of 2006 and in 2007. We cannot provide assurance that the recent increase in revenue will continue in the future, as we believe businesses may continue to be reluctant to significantly increase spending on enterprise communications systems in the near future. In addition, we believe some uncertainty exists in the marketplace caused by the transition of communication systems from circuit-switch to packet-switch architectures, including voice over Internet Protocol (VoIP) systems, and this uncertainty may cause some organizations to delay making investments in new systems.

We believe that enterprises continue to be concerned about their ability to increase revenues and profitability, in part due to the continued uncertain economic environment and slowdown in the past few years. To maintain or improve profitability, we believe that businesses have attempted to reduce costs and capital spending. We expect continued pressure on our ability to generate or expand sales and it is not clear whether business communications spending will increase in the near term. We cannot predict the nature, timing and extent of future business investments in communications systems and as a result, if and when our net sales will increase.

The markets in which we compete have been characterized by rapid technological changes and increasing customer requirements. We have sought to address these requirements through the development of software enhancements and improvements to existing systems and the introduction of new systems, products, and applications. Research and development expenses increased 1.0% to $8.8 million, or 7.6% of net sales in the second quarter of 2006, compared to $8.7 million, or 7.6% of net sales in the second quarter of 2005. We expect that research and development expenses may vary in absolute dollars and as a percentage of net sales relative to the prior year as we continue to develop new technologies and products and enhance existing systems and products. Inter-Tel's research and development efforts over the last several years have been focused primarily on the development of converged systems and software, including the Inter-Tel 5000 series and LAN-enabled telephony platforms including the Inter-Tel 7000 series, as well as contact center, presence management and collaboration software and applications, and the development and cost reduction of SIP (Session Initiation Protocol) and IP (Internet Protocol) endpoints and technology. In addition, we have continued the development of, and enhancements to, our *Axxess* system, including adding new applications, enhancing and developing new IP convergence capabilities and applications, and developing Unified Communications applications.

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We offer our customers a package of lease financing and other managed services under the name TotalSolution. TotalSolution provides our customers lease financing, maintenance and support services, fixed price upgrades and other benefits. We finance this program through the periodic resale of lease rental streams to financial institutions. Refer to Note E of Notes to Condensed Consolidated Financial Statements for additional information regarding our TotalSolution program.

**Results of Operations**

The following table sets forth certain statement of operations data expressed as a percentage of net sales for the periods indicated:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2006 | 2005 | 2006 | 2005 |
| **NET SALES** | | | | |
| Telecommunications systems, software and related | 87.1% | 88.2% | 86.7% | 88.0% |
| Resale of local, long distance and network services | 12.9 | 11.8 | 13.3 | 12.0 |
| **TOTAL NET SALES** | 100% | 100.0% | 100% | 100.0% |
| **COST OF SALES** | | | | |
| Telecommunications systems, software and related | 42.8 | 40.7 | 42.2 | 40.9 |
| Resale of local, long distance and network services | 8.2 | 7.2 | 8.4 | 7.5 |
| **TOTAL COST OF SALES** | 51.0 | 47.9 | 50.6 | 48.4 |
| **GROSS PROFIT** | 49.0 | 52.1 | 49.4 | 51.6 |
| Research and development | 7.6 | 7.6 | 7.7 | 7.8 |
| Selling, general and administrative | 34.7 | 34.9 | 35.3 | 35.8 |
| Amortization of intangibles | 1.0 | 1.0 | 1.0 | 0.9 |
| Write-off of in-process research and development costs | — | — | — | 1.2 |
| **Legal judgment and settlement** | — | — | 0.6 | — |
| **OPERATING INCOME** | 5.7 | 8.6 | 4.8 | 6.1 |
| Interest and other income | 1.3 | 0.8 | 1.3 | 0.8 |
| Foreign currency transaction (losses) gains | (0.3) | 0.1 | (0.2) | 0.1 |
| Interest expense | (0.0) | 0.0 | (0.0) | 0.0 |
| **INCOME BEFORE INCOME TAXES** | 6.7 | 9.5 | 5.8 | 6.9 |
| **INCOME TAXES** | 2.6 | 3.5 | 2.3 | 2.9 |
| **NET INCOME** | 4.1% | 6.0% | 3.6% | 4.0% |

*Net Sales.* Net sales increased 0.6%, or $0.7 million, to $115.9 million in the second quarter of 2006 from $115.3 million in the second quarter of 2005. Net sales increased 0.9%, or $1.9 million, to $222.8 million in the first six months of 2006 from $220.9 million in the first six months of 2005. Excluding the Lake acquisition in the first quarter of 2005, net sales decreased 0.3%, or $0.7 million, for the first six months of 2006 compared to net sales for the corresponding prior year period. We acquired Lake in March 2005, and accordingly generated revenues for only four of the first six months of 2005. Sales attributable to our dealer network decreased 1.3%, or $0.3 million in the second quarter of 2006, and increased 0.3%, or $0.1 million in the first six months of 2006 compared to the corresponding periods in 2005. Sales from our direct sales offices (including revenues from lease financing) decreased 8.5%, or $5.0 million, in the second quarter of 2006, and 9.5%, or $11.0 million, in the first six months of 2006 compared to the corresponding periods in 2005. This decrease was primarily due to lower sales volumes and smaller system sales through our direct sales offices and a lower volume of financed sales from our captive leasing company. These decreases were more than offset by increases in DataNet, International

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Divisions, national, government and education accounts, and local and long distance network services. Sales from our DataNet division, which sells networking products through our direct sales offices, national, government and education accounts division and dealer channel, increased 79.4%, or $2.8 million, in the second quarter of 2006 and 48.4%, or $3.3 million, in the first six months of 2006 compared to the corresponding periods in 2005. International revenues increased 9.1%, or $1.0 million in the second quarter of 2006, and 25.2%, or $4.3 million in the first six months of 2006 compared to the corresponding periods in 2005. This increase in international net sales during the second quarter was attributable to increased sales in the UK and Swan divisions, offset in part by a decrease in sales from our Lake operations compared to the same period in 2005. International revenues excluding the Lake acquisition increased 25.5%, or $1.6 million for the first six months of 2006.

Sales from our national, government and educational accounts increased by 14.5%, or $0.7 million in the second quarter of 2006 and 22.5%, or $2.2 million, in the first six months of 2006 compared to the corresponding periods in 2005. These increases were largely attributable to the increase in sales dollars from the additional sales representatives added in 2005. Sales from local and long distance and network services division (NSG), which includes Inter-Tel NetSolutions® (NetSolutions) and Network Services Agency (NSA), increased 10.2%, or $1.4 million, in the second quarter of 2006 and 11.7%, or $3.1 million, for the first six months of 2006, compared to the corresponding periods in 2005. Sales from NetSolutions increased 9.9%, or $1.2 million in the second quarter of 2006, and 10.6% or $2.6 million for the first six months of 2006 compared to the corresponding periods in 2005. This continued an upward trend of sales despite downward price pressure and significant competition. Sales from NSA, a commission-based sales unit within the local, long distance resale and network services division acting as an agent to sell services for selected RBOC's and CLEC's, increased 13.3%, or $0.2 million in the second quarter of 2006 and 23.4%, or $0.5 million for the first six months of 2006 compared to the corresponding periods in 2005.

We released our Inter-Tel 5000 v2.0 software and Inter-Tel 5600 late in the second quarter of 2006. The release of these products has had very little impact on our revenue for the second quarter of 2006. Based upon feedback from our direct sales offices, dealers and end users, we expect a greater impact on sales from these products starting in the third quarter of 2006.

*Gross Profit.* Gross profit for the second quarter of 2006 decreased 5.5% to $56.8 million, or 49.0% of net sales, from $60.0 million, or 52.1% of net sales, in the second quarter of 2005. Gross profit for the first six months of 2006 decreased 3.5% to $110.0 million, or 49.4% of net sales, from $114.0 million, or 51.6% of net sales, in the corresponding period of 2005. The decrease in gross profit dollars and gross profit as a percentage of sales in the second quarter of 2006 was primarily due to selling fewer larger line size systems, which traditionally have a higher software content, the product and distribution mix and product transition on the new 5000 series products resulting in lower margins, as well as industry pricing pressures, leading to some limited sales promotions and discounts on product and services. From a product and distribution mix perspective, the gross margin percentage was affected by higher percentages of net sales recognized in our local, long distance and network services divisions, national, government and education accounts divisions, DataNet operations and international operations, which typically generate lower gross margins than other divisions within our operating principal segment. In addition, the increase in the dollar amount of the cost of goods sold was attributable to the higher volume of net sales from our DataNet and international operations and product transition to our new 5000 series products resulting in higher equipment costs. Sales through our dealer channel were relatively flat during the three and six months ended June 30, 2006, compared to comparable periods in 2005. The decrease in gross profit dollars and gross profit as a percentage of sales in the six months ended June 30, 2006 compared to 2005 was primarily attributable to product and distribution mix as discussed above, as well as industry pricing pressures, leading to some limited sales promotions and discounts on product and services. Cost of goods sold was impacted only slightly in the second quarter of 2006 due to FAS 123R related costs associated with expensing of the value of stock options and employee stock purchase plan shares.

During the second quarter of 2006, recurring revenues decreased slightly as a percentage of net sales from existing customers in our direct sales, DataNet and national and government accounts channels relative to the same channels in the second quarter of 2005. We generally recognize higher gross margins for recurring revenues in these operations. Existing customers accounted for a significant portion and higher relative component of our net sales from maintenance and other services, software

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additions and/or upgrades, and other peripheral products, such as video conferencing, call logging solutions, wireless endpoints, power protection, wired and wireless headsets, audio conferencing units and networking products, during the second quarter and first six months of 2006. Our business communications platforms allow for system migration without the complete replacement of hardware, enabling us to offer enhancements and new solutions through software-only upgrades to our existing customers. Consequently, our gross margins are generally higher with recurring revenues because we incur less materials costs relative to new installations.

Sales from NetSolutions increased by 9.9%, or $1.2 million in the second quarter of 2006, and 10.6% or $2.6 million for the first six months of 2006, compared to the corresponding periods in 2005. Gross margins are generally lower in this division than our consolidated margins. Sales from Network Services Agency, increased 13.3%, or $0.2 million, in the second quarter of 2006 and 23.4%, or $0.5 million for the first six months of 2006 compared to the corresponding periods in 2005. This division generally receives commissions on network services we sell as an agent for Regional Bell Operating Companies. Sales from this division carry little to no equipment costs and generated margins of 90.1% during the second quarter of 2006. Accordingly, the increase in sales from this division offset in part our decrease in consolidated gross profit percentage.

We cannot accurately predict future consolidated gross margins because of period-to-period variations in a number of factors, including among others, competitive pricing pressures, sales of systems, software and services through different distribution channels, supplier and agency agreements, and the mix of systems, software and services we sell, as well as market acceptance of new products.

*Research and Development.* Research and development expenses for the second quarter of 2006 increased 1.0% to $8.8 million, or 7.6% of net sales, from $8.7 million, or 7.6% of net sales, for the second quarter of 2005. The increase was attributable to expenses associated with FAS 123R expensing of stock options, which totaled $282,000 during the quarter ended June 30, 2006. Excluding FAS 123R expenses, R&D expenses decreased 2.3%, or $0.2 million, in the quarter ended June 30, 2006 compared to the corresponding period in 2005. The decrease in R&D spending, excluding FAS 123R costs, during the second quarter of 2006 compared to 2005 was primarily the result of lower costs associated with third-party development costs and lower relative project costs, offset in part by increased costs incurred in connection with beta sites prior to the introduction of new products. In the six months ended June 30, 2006, R&D expenses decreased slightly to $17.1 million compared to $17.2 million in the first six months of 2005. Excluding FAS 123R expenses, R&D expenses would have totaled $16.5 million in the first six months of 2006, a decrease of 3.7% compared to the corresponding period in 2005. In the second quarter ended June 30, 2006, research and development expenses were directed principally toward the continued development of converged systems and software, including version 2.0 of the Inter-Tel 5000 systems and software, the Inter-Tel 5600, Inter-Tel 7000 software and systems, contact center, presence and collaboration applications, and IP endpoint development. We expect that research and development expenses may vary in absolute dollars and as a percentage of net sales relative to the prior year as we continue to develop and enhance existing and new technologies and products.

*Selling, general and administrative.* In the second quarter of 2006, selling, general and administrative expenses decreased 0.2% to $40.2 million, or 34.7% of net sales, from $40.3 million, or 34.9% of net sales, in the second quarter of 2005, despite the increase in net sales during the same period. For the six months ended June 30, 2006 selling, general and administrative expenses decreased 0.3% to $78.7 million, or 35.3% of net sales, from $79.0 million or 35.8% of net sales, compared to the corresponding period in 2005. We incurred significant costs during the quarter and six months ended June 20, 2006 associated with the recent proxy contest and ongoing expenses incurred in connection with the Company's response to the unsolicited interest of Steven G. Mihaylo (the Company's former Chief Executive Officer and current board member) and affiliated parties to acquire the Company. We have incurred and continue to incur extensive professional fees, investment banking advisory fees, legal expenses, director fees and payments to directors in lieu of stock options, and related costs (collectively, "proxy contest and related costs"). SG&A expenses in the second quarter of 2006 included FAS 123R expenses and proxy contest and related costs totaling $2.4 million. Excluding these costs, SG&A would have totaled $37.8 million, or 32.6% of net sales in the second quarter of 2006, a decrease of 6.0% from the second quarter of 2005. SG&A expenses in the six months ended June 30, 2006 included FAS 123R expenses, legal expenses incurred in the first quarter of 2006 associated with a legal settlement recorded

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in the fourth quarter of 2005, and proxy battle related costs totaling $3.1 million. Excluding these costs, SG&A for the first six months of 2006 was $75.7 million, or 34% of net sales, a decrease of 4.2% from the first six months of 2005.

The decrease in absolute dollars (excluding the items noted above) was primarily attributable to reduced selling expenses and a lower number of personnel and compensation costs in our direct sales offices. The number of personnel included in SG&A decreased by 97 at June 30, 2006 compared to June 30, 2005, and decreased 111 on a company-wide basis during the same time period. Bad debt expense also decreased 56.6% in the second quarter of 2006 compared to the second quarter of 2005 and 35.6% for the first six months of 2006 compared to the first six months of 2005. During 2006, we incurred an increase in professional fees, including higher legal and accounting costs. Marketing expenses increased slightly in the second quarter of 2006 compared to the second quarter of 2005. In the foreseeable future we will incur additional marketing expenses with the introduction of the Inter-Tel 5600 and the anticipated release of the Inter-Tel 7000 platform. The increase in SG&A was also attributable in part to additional legal costs incurred and to implement and maintain a more comprehensive corporate compliance program in connection with our E-Rate settlement. We expect that for the foreseeable future selling, general and administrative expenses may vary in absolute dollars and as a percentage of net sales.

*Amortization of purchased intangible assets.* We adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142") effective in the beginning of fiscal 2002. In accordance with SFAS 142, we ceased amortizing goodwill. We are required to perform goodwill impairment tests on an annual basis and between annual tests in certain circumstances. As of June 30, 2006, no impairment of goodwill has been recognized in 2006. We face the risk that future goodwill impairment tests may result in charges to earnings.

Amortization of purchased intangible assets included in operating expenses was $1.2 million in the second quarter of 2006, compared to $1.1 million in the second quarter of 2005. In addition, $5,000 of amortization was included in research and development expenses for the second quarter of 2006, compared to $55,000 in the second quarter of 2005. Amortization of purchased intangible assets included in operating expenses was $2.3 million in the six months ended June 30, 2006, compared to $1.9 million for the same period in 2005. In addition, $10,000 of amortization was included in research and development expenses for the first six months of 2006, compared to $110,000 in the same period in 2005. The increase in the amortization of purchased intangible assets for the second quarter and first six months of fiscal 2006 compared to the same periods in 2005 was primarily related to the additional amortization associated with purchased technology that was placed in service in 2006, and thus amortizable in 2006. For additional information regarding purchased intangible assets, see Note C "Acquisitions" to the Condensed Consolidated Financial Statements.

*Write-off of in-process research and development (IPRD) costs.* During the first quarter of 2005, Inter-Tel completed the acquisition of Lake (see NOTE C). The aggregate purchase price of the Lake acquisition was allocated to the fair value of the assets and liabilities acquired, of which $2.6 million, or $0.10 per diluted share, was written-off as purchased IPRD.

*Interest and Other Income.* Interest and other income in 2006 and 2005 consisted primarily of interest income and foreign currency transaction gains or losses. The net increase in interest and other income of $621,000 in the second quarter of 2006 compared to the corresponding period in 2005 was due primarily to higher levels of invested funds, as well as higher rates of return. Foreign currency transaction losses in the first six months of 2006 were $362,000 compared to gains of $141,000 in the first six months of 2005. Interest expense was nominal in both periods, but interest expense decreased $11,000 in the first six months of 2006 compared to the first six months of 2005.

*Income Taxes.* Inter-Tel's income tax rate for the second quarter of 2006 was 38.4% compared to 36.6% for the second quarter of 2005, and 38.7% in the first six months of 2006 compared to 42.0% for the same period in 2005. The increase in the rate for the second quarter was primarily attributable to the

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expiration of the research credit and the adoption of SFAS 123R offset by the 2005 write-off of in-process research and development costs in connection with our Lake acquisition and the accrual for non-deductible expenses anticipated in connection with GSA contract pricing and trade agreement issues discovered during the second quarter of 2005. Inter-Tel currently expects the full-year 2006 tax rate to be approximately 38% to 40%, subject to prospective changes in the tax laws or other factors, including the potential extension of the research and development credit, and the relative level of tax-exempt investments to total funds available for investment. Excluding the effect of SFAS 123R and the effect of the proxy contest and related costs, the tax rate for the first six months of 2006 was approximately 36.8%. The 2006 rate is subject to change based on the projected results of operations and other factors identified above.

*Net Income*. Net income for the second quarter of 2006 was $4.8 million ($0.18 per diluted share), a decrease of 31.1% compared to net income of $6.9 million ($0.26 per diluted share) in the second quarter of 2005. Net income for the six months ended June 30, 2006 was $8.0 million ($0.29 per diluted share), a decrease of 10.3% compared to net income of $8.9 million ($0.32 per diluted share) for the six months ending June 30, 2005.

The decrease in net income for the quarter and for the first six months of 2006 compared to the corresponding period in 2005 was primarily attributable to SFAS 123R expenses, fees and expenses associated with the ongoing proxy contest, and additional fees and costs associated with a legal settlement recorded in the fourth quarter of 2005. Such additional fees and expenses totaled approximately $1.9 million after taxes ($0.07 per diluted share) and $3.4 million after taxes ($0.13 per diluted share) for the three and six months ended June 30, 2006, respectively. Additional information regarding these and other items is described in further detail above.

**Inflation/Currency Fluctuation**

Inflation and currency fluctuations have not previously had a material impact on Inter-Tel's operations. Inter-Tel's International procurement agreements have traditionally been denominated in U.S. currency. Moreover, a significant amount of contract manufacturing has been or may be moved to alternative sources. The expansion of international operations in the United Kingdom and Europe, and increased international sales, if any, as a result of the 2005 Lake acquisition could result in higher international sales as a percentage of total revenues. This may increase the Company's risks relating to currency fluctuations.

**Liquidity and Capital Resources**

| | Six Months Ended June 30, | |
|---|---|---|
| (In thousands) | 2006 | 2005 |
| Net cash provided by operating activities | $ 13,213 | $ 12,066 |
| Net cash used in investing activities | (3,561) | (32,283) |
| Net cash (used in) provided by financing activities | 1,216 | (37,571) |
| Effect of exchange rate changes | 1,390 | (524) |
| Increase (decrease) in cash and equivalents | 12,258 | (58,312) |
| Cash and equivalents at beginning of period | 103,774 | 152,330 |
| Cash and equivalents at end of period | $116,032 | $ 94,018 |

At June 30, 2006, cash and equivalents ($116.0 million) and short-term investments ($63.9 million) totaled $179.9 million, which represented an increase of approximately $12.5 million from the balance at December 31, 2005. We maintain a $10 million unsecured, revolving line of credit that is available through June 30, 2007. Under the credit facility, we have the option to borrow at a prime rate or adjusted LIBOR interest rate. Historically, we have used the credit facility primarily to support international letters of credit to suppliers. As of June 30, 2006, none of the credit line was used. The remaining cash balances may be used for acquisitions, strategic alliances, working capital, dividends, common stock repurchases and general corporate purposes.

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Net cash provided by operating activities totaled $13.2 million for the six months ended June 30, 2006, compared to $12.1 million for the corresponding period in 2005. Cash provided by operating activities in the first six months of 2006 primarily resulted from net income plus non-cash charges for depreciation and amortization expenses, provisions for losses, and share based compensation expenses, offset in part by excess tax benefits from stock options exercised, decrease in other liabilities, deferred income taxes and changes in operating assets and liabilities. Cash provided by operating activities in the first six months of 2005 was primarily the result of cash generated from profitable operations, adding back non-cash items such as depreciation, amortization, purchased research and development and provision for losses offset by an $11.4 million change in operating assets and liabilities (including E-Rate settlement of $8.5 million). Cash used by the change in operating assets and liabilities totaled $3.3 million in the first six months of 2006 primarily due to increases in receivables, inventories and prepaid expenses and other assets, partially offset by decreases in income taxes receivable and deferred income taxes, as well as increases in accounts payable and other current liabilities. We expect to expand sales through our direct sales offices and dealer networks, which is expected to require the expenditure of working capital for increased accounts receivable, inventories and net investment in sales-leases.

Net cash used in investing activities totaled $3.6 million for the six months ended June 30, 2006, compared to cash used in investing activities of $32.3 million for the six months ended June 30, 2005. The change from 2005 to 2006 was primarily a result of $27.8 million in cash used for acquisitions in the first six months of 2005 where as minimal cash has been used for acquisitions in 2006. Cash used to purchase available for sale investments totaled $38.8 million in the first six months of 2006, offset by $38.6 million in maturities and sales of available for sale investments. Cash used for capital expenditures totaled $3.4 million in the first six months of 2006 and $4.3 million for the corresponding period in 2005.

Net cash provided by financing activities totaled $1.2 million for the six months ended June 30, 2006, compared to cash used in financing activities of $37.6 million for the corresponding period in 2005. Net cash used for cash dividends, including a special $1.00 per share dividend in 2005 only, totaled $30.7 million in the first six months of 2005 compared to $4.2 million in the same period for 2006. During the second quarter of 2005, the Company expended $13.8 million to repurchase 716,500 shares of the Company's common stock pursuant to a stock repurchase program under which the Board of Directors authorized the repurchase of up to $75 million of the Company's common stock. The Company's stock repurchases in the second quarter of 2005 were funded primarily by existing cash balances. Net cash provided by proceeds from the exercise of stock options and Employee Purchase Plan (ESPP) shares totaled $4.4 million in the first six months of 2006 compared to $6.9 million in the same period for 2005. During the first six months of 2006 and 2005 we reissued treasury shares through stock option issuances, with the proceeds received totaling less than the cost basis of the treasury stock reissued. Accordingly, the difference was recorded as a decrease to retained earnings of $1.5 million and $1.6 million, in 2006 and 2005, respectively.

We offer to our customers lease financing and other services, including our TotalSolution (formerly Totalease) program, through our Inter-Tel Leasing, Inc. subsidiary. We fund our TotalSolution program in part through the sale to financial institutions of rental payment streams under the leases. Sold lease rentals totaling $272.3 million and $270.3 million remained unbilled at June 30, 2006 and December 31, 2005, respectively. We are obligated to repurchase such income streams in the event of defaults by lease customers and, accordingly, maintain reserves based on loss experience and past due accounts. Although, to date, we have been able to resell the rental streams from leases under the TotalSolution program profitably and on a substantially current basis, the timing and profitability of lease resales could impact our business and operating results, particularly in an environment of fluctuating interest rates and economic uncertainty. If we are required to repurchase rental streams and realize losses thereon in amounts exceeding our reserves, our operating results will be adversely affected.

During 2006, the Company has entered into "rate-lock" agreements with a financial institution in the form of commitments to sell the cash flow streams for leases at a fixed interest rate to the financial institution. As of June 30, 2006, the Company has one outstanding agreement in place to sell cash flow streams with a present value of $15.0 million in December 2006 at a fixed interest rate to a financial

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institution. As part of the agreement, the Company has the option to pay $300,000 to the financial institution to cancel the commitment. Subsequent to June 30, 2006, the Company entered into another agreement to sell cash flow streams with a present value of $10.0 million in March 2007 at a fixed interest rate to a financial institution. As part of the agreement, the Company has the option to pay $100,000 to the financial institution to cancel the commitment.

In addition, on January 21, 2005, Inter-Tel Technologies received notification from the Federal Communications Commission that the Technologies subsidiary was temporarily suspended from participation in the E-Rate program pending a final hearing to determine a possible debarment of three (3) years or more. Technologies contested the scope and length of the proposed debarment from the E-Rate program. The Company was notified on June 30, 2006 that on or about June 21, 2006, the FCC issued its final decision on the matter and imposed upon the Technologies subsidiary a debarment from the E-Rate program of one (1) year from June 30, 2006. Reasons for the shorter period were, among other factors, that Technologies had instituted a compliance program and been cooperative in the investigation and ongoing hearings with the Department of Justice. The FCC order further clarified that the parent and other subsidiaries were not debarred. The Company recorded no revenues since January 21, 2005 relating to Inter-Tel Technologies' participation in the E-Rate program.

During the second quarter of 2005, we identified variances in our sales processes as they relate to certain terms included in the U.S. General Services Administration (GSA) pricing and trade agreement requirements applicable to our business. As a result of this identification, Inter-Tel made voluntary self-disclosure of the matter to the Inspector General of the GSA. The potential variances relate primarily to noncompliance with certain pricing thresholds and noncompliance with trade agreements that are applicable to transactions with certain government agencies. We continue to monitor our compliance and have taken appropriate corrective measures with respect to these potential variances. In the second quarter of 2005, we accrued $1.8 million in estimated pre-tax adjustments, including reductions in net sales and increases to costs, fines and penalties that may be incurred to correct this issue, of which we have paid $1.2 million through June 30, 2006. Our estimate at June 30, 2006 remains the same as the total identified as of the end of the second quarter of 2005. The total sales potentially subject to the GSA agreements were approximately $5.5 million during the period from March 28, 2001 through June 10, 2005. Our current contract with the GSA expires in August 2006, and we have requested and expect to receive an extension of that contract.

In the first quarter of 2006, the Company settled another legal matter in connection with a longstanding dispute with a former international dealer that existed as of December 31, 2005. The Company recorded an accrual for the settlement amount and related fourth quarter legal fees as of December 31, 2005. The settlement plus related fourth quarter legal fees totaled $1.6 million. Additional legal fees totaling approximately $1.3 million were recorded as period costs during the first quarter of 2006 relating to this matter.

On June 16, 2006, a shareholder class action suit was filed against Inter-Tel and selected Board members in Delaware state court. On June 16 and June 20, 2006, respectively, two additional shareholder class actions against the Company and each of its Board members were filed in Arizona state court. The Delaware action, as amended July 14, 2006, raises claims related to the reincorporation filing by Inter-Tel in Delaware and primarily seeks injunctive relief. The Arizona actions claim breach of fiduciary duty related to the 13D filings by the Company's former CEO. The Company is in the process of evaluating these class action suits.

We believe our working capital and credit facilities, together with cash generated from operations, will be sufficient to develop and expand our business operations, to finance acquisitions of additional resellers of telephony products and other strategic acquisitions or corporate alliances, to fund quarterly dividends to shareholders, to repurchase additional shares of the Company's common stock pursuant to the Board-approved $75 million repurchase program, of which $61.2 million remains authorized, and to provide adequate working capital for the foreseeable future. However, to the extent additional funds are required in the future to address working capital needs and to provide funding for capital expenditures, expansion of the business or additional acquisitions or share repurchases, we will seek additional financing. There can be no assurance additional financing will be available when required or on acceptable terms.

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**Off-Balance Sheet Arrangements**

As part of our ongoing business, we do not participate in transactions that involve unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. However, we offer to our customers lease financing and other services through our Inter-Tel Leasing, Inc. subsidiary. We fund our TotalSolution program in part through the sale to financial institutions of rental payment streams under the leases. Such financial institutions have the option to require us to repurchase such income streams, subject to limitations, in the event of defaults by lease customers and, accordingly, we maintain reserves based on loss experience and past due accounts. For more information regarding our lease portfolio and financing, please see "Liquidity and Capital Resources" and Note E of Notes to Condensed Consolidated Financial Statements.

**Critical Accounting Policies and Estimates**

The methods, estimates and judgments we use in applying our most critical accounting policies have a significant impact on the results we report in our condensed consolidated financial statements. We evaluate our estimates and judgments on an on-going basis. We base our estimates on historical experience and on assumptions that we believe to be reasonable under the circumstances. Our experience and assumptions form the basis for our judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may vary from what we anticipate and different assumptions or estimates about the future could change our reported results. We believe the following accounting policies are the most critical to us, in that they are important to the portrayal of our financial statements and they require our most difficult, subjective or complex judgments in the preparation of our condensed consolidated financial statements:

*Revenue Recognition.* In December 2003, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 104 (SAB 104), "Revenue Recognition." The Company applies the provisions of SAB 104 to all revenue transactions. SAB 104 supersedes SAB 101, "Revenue Recognition in Financial Statements." The primary purpose of SAB 104 is to rescind accounting guidance contained in SAB 101 related to multiple element revenue arrangements, superseded as a result of the issuance of EITF 00-21. Additionally, SAB 104 rescinded the SEC's Revenue Recognition in Financial Statements Frequently Asked Questions and Answers ("the FAQ") issued with SAB 101 that had been codified in SEC Topic 13, Revenue Recognition. Selected portions of the FAQ have been incorporated into SAB 104. While the wording of SAB 104 has changed to reflect the issuance of EITF 00-21, the revenue recognition principles of SAB 101 remain largely unchanged by the issuance of SAB 104. The issuance of SAB 104 did not have a material impact on the Company's financial position, results of operations or cash flows.

*End-user sales through our direct sales offices and government and national accounts division.* Revenue is recognized when all four of the following criteria are met: (i) persuasive evidence that arrangement exists; (ii) delivery of the products and/or services has occurred; (iii) the selling price is both fixed and determinable and; (iv) collectibility is reasonably probable. Revenue derived from sales of systems and services to end-user customers is recognized upon primary installation of the systems and performance of the services, respectively, allowing for use by our customers of these systems. Pre-payments for communications services are deferred and recognized as revenue as the communications services are provided. We do not generally allow sales returns either by the terms of our contracts or in practice, except for returns related to warranty provisions.

*Dealer and VAR sales.* For shipments to dealers and other distributors, our revenues are recorded as products are shipped and services are rendered, when the sales process is complete. These shipments are primarily to third-party dealers and distributors, and title passes when goods are shipped (free-on-board shipping point). However, in connection with our recent Lake acquisition, shipments to one international dealer are initially held by that dealer on a consignment basis. Such inventory is owned by Inter-Tel and reported on Inter-Tel's books and records until the inventory is sold to third parties, at which time the revenue is recorded. We do not generally allow sales returns either by the terms of our contracts or in practice, except for returns related to warranty provisions. We provide a number of incentives, promotions and awards to certain dealers and other distributors. These incentives primarily represent

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discounts (which are recognized as a reduction of sales), advertising allowances and awards (which are recognized as marketing expense) and management assistance (which is expensed as incurred).

*Resale of long distance.* We recognize revenue from long distance resale services as services are provided.

*Maintenance revenues.* We recognize maintenance revenue ratably over the term of applicable maintenance agreements.

*Sales-Leases.* For our sales-type lease accounting, we follow the guidance provided by FASB Statement No. 13, Accounting for Leases and FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities – A Replacement of FASB Statement No. 125. We record the discounted present values of minimum rental payments under sales-type leases as sales, net of provisions for continuing administration and other expenses over the lease period. We record the lease sales at the time of system sale and installation pursuant to Staff Accounting Bulletin No. 104, as discussed above for sales to end user customers. The costs of systems installed under these sales-leases are recorded as costs of sales. The net rental streams are sold to funding sources on a regular basis with the income streams discounted by prevailing like-term rates at the time of sale. Gains or losses resulting from the sale of net rental payments from such leases are recorded as net sales. We establish and maintain reserves against potential recourse following the resales based upon historical loss experience, past due accounts and specific account analysis. The allowance for uncollectible minimum lease payments and recourse liability at the end of the year represents reserves against the entire lease portfolio. Management reviews the adequacy of the allowance on a regular basis and adjusts the allowance as required. These reserves are either netted in the accounts receivable, current and long-term components of "Net investments in Sales-Leases" on the balance sheet, or included in long-term liabilities on our balance sheet for off-balance sheet leases.

Historically, our reserves have been adequate to cover write-offs. Our total reserve for losses related to the entire lease portfolio, including amounts classified as accounts receivable in our balance sheet, decreased from 5.36% at December 31, 2005 to 5.32% at June 30, 2006, primarily as a result of reviews of our write-off experience and accounts receivable agings. Should the financial condition of our customers deteriorate in the future, additional reserves in amounts that could be material to the financial statements could be required.

*Goodwill and Other Intangible Assets.* On January 1, 2002, Inter-Tel adopted SFAS No. 141, *Business Combinations*, and SFAS No. 142, *Goodwill and Other Intangible Assets.* Purchase prices of acquired businesses that are accounted for as purchases have been allocated to the assets and liabilities acquired based on the estimated fair values on the respective acquisition dates. Based on these values, the excess purchase prices over the fair value of the net assets acquired were allocated to goodwill.

Prior to January 1, 2002, Inter-Tel amortized goodwill over the useful life of the underlying asset, not to exceed 40 years. On January 1, 2002, Inter-Tel began accounting for goodwill under the provisions of SFAS Nos. 141 and 142 and discontinued the amortization of goodwill after January 1, 2002. As of June 30, 2006, Inter-Tel had gross goodwill of $34.9 million and accumulated amortization of $5.0 million. Inter-Tel completed one acquisition through June 30, 2006 and one in 2005 and has not recorded any amortization for these acquisitions on amounts allocated to goodwill in accordance with SFAS No. 141.

The Company performs an annual impairment test on Goodwill using the two-step process prescribed in SFAS No. 142. The first step is a screen for potential impairment, while the second step measures the amount of the impairment, if any. In addition, the Company will perform impairment tests during any reporting period in which events or changes in circumstances indicate that an impairment may have incurred. Inter-Tel performed the first step of the required impairment tests for goodwill as of December 31, 2005 and determined that goodwill is not impaired and it is not necessary to record any impairment losses related to goodwill. At June 30, 2006 and December 31, 2005, $27.7 million of the Company's goodwill, net of amortization, relates to the Company's principal segment and $2.1 million relates to the Resale of Local, Long Distance and Network Services segment. There is only one reporting unit (i.e., one component) as defined in paragraph 30 of SFAS 142 within each of the Company's two operating segments as defined in paragraph 10 of SFAS 131. Therefore the reporting units are identical to

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the segments. Fair value has been determined for each segment in order to determine the recoverability of the recorded goodwill. At December 31, 2005, the Company used two tests in determining that no impairment had occurred. One test is an allocation of the market capitalization of the entire company using average common stock prices and one test is based on a calculation of the cash flows for each reporting unit. Both tests resulted in values that exceeded the net carrying value of the reporting units. Therefore, the second step for potential impairment was unnecessary.

The Company evaluates the remaining useful lives of its purchased intangible assets, all of which are subject to amortization, each reporting period. Any changes to estimated remaining lives prospectively effect the remaining period of amortization. In addition, the purchased intangible assets are reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. A loss would be recognized for any excess of the carrying amount over the estimated fair value. As of June 30, 2006, Inter-Tel had gross purchased intangible assets of $36.1 million and accumulated amortization of $14.8 million.

At June 30, 2006 and December 31, 2005, goodwill, net of accumulated amortization, totaled $29.8 million. Other acquisition-related intangibles, net of accumulated amortization, totaled $21.3 million at June 30, 2006 and $23.7 million at December 31, 2005. Accumulated amortization through June 30, 2006 was $19.8 million, including $5.0 million of accumulated amortization attributable to goodwill and $14.8 million of accumulated amortization of other acquisition-related intangibles. Accumulated amortization through December 31, 2005 was $17.5 million, including $5.0 million of accumulated amortization attributable to goodwill and $12.5 million of accumulated amortization of other acquisition-related intangibles. Other acquisition-related intangibles, comprised primarily of developed technology (5-10 year lives), customer lists (5-8 year lives) and non-competition agreements (2-8 year lives), are amortized on a straight-line basis. The useful lives for developed technology are based on the remaining lives of patents acquired or the estimated useful life of the technology, whichever is shorter. The useful lives of the customer lists are based on the expected period of value for such lists. The useful lives for non-competition agreements are based on the contractual terms of the agreements.

*Allowance for Doubtful Accounts*. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. Additional reserves or allowances for doubtful accounts are recorded for our sales-type leases, discussed above in "Sales-Leases." We establish and maintain reserves against estimated losses based upon historical loss experience, past due accounts and specific account analysis. Management reviews the level of the allowances for doubtful accounts on a regular basis and adjusts the level of the allowances as needed. In evaluating our allowance we consider accounts in excess of 60 days old as well as other risks in the more current portions of the accounts included. At June 30, 2006, our allowance for doubtful accounts for accounts receivable were $6.3 million of our $55.9 million in gross accounts receivable. If the financial condition of our customers or channel partners were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

*Inventories*. We value our inventories at the lower of cost (principally on a standard cost basis, which approximates the first-in, first-out (FIFO) method) or market. Significant management judgment is required to determine the reserve for obsolete or excess inventory and we make our assessment primarily on a significant product-by-product basis for the immediately preceding twelve-month period, adjusted for expected changes in projected sales or marketing demand. Inventory on hand may exceed future demand either because the product is outdated or obsolete, or because the amount on hand is more than can be used to meet estimated future needs. We consider criteria such as customer demand, product life cycles, changing technologies, slow moving inventory and market conditions and we reserve for our excess and possible obsolete inventory. Historically, sales of scrap have not been material and have not affected our profit margins. If actual customer demand, product life cycles, changing technologies and market conditions are less favorable than those projected by management, additional inventory reserves may be required in the future.

*Contingencies*. We are a party to various claims and litigation in the normal course of business. Management's current estimated range of liability related to various claims and pending litigation is based on claims for which management can estimate the amount and range of loss, or can estimate a minimum amount of a loss. Because of the uncertainties related to both the amount and range of loss on the

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remaining pending claims and litigation, management is unable to make a reasonable estimate of the liability that could result from an unfavorable outcome. As additional information becomes available, we will assess the potential liability related to our claims and pending litigation, revise our estimates and accrue for any losses to the extent that they are probable and the amount is estimable. Such revisions in our estimates of the potential liability could materially impact our results of operations and financial position. However, at June 30, 2006, management did not believe that the ultimate impact of various claims and pending litigation would have a materially adverse impact on the results of operations, liquidity or financial condition of the Company. Refer to Note A to the Condensed Consolidated Financial Statements for details of specific contingencies.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The following discussion about our market risk disclosures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. We are exposed to market risk related to changes in interest rates and foreign currency exchange rates. We do not use derivative financial instruments.

INVESTMENT PORTFOLIO. We do not use derivative financial instruments in our non-trading investment portfolio. Inter-Tel maintains a portfolio of highly liquid cash equivalents. Inter-Tel places its investments in instruments that meet high credit quality standards, as specified in our investment policy guidelines.

The Company also maintains short-term investments. Those investments that are classified as available for sale have been recorded at fair value, which approximates cost. Those investments that are classified as held-to-maturity have been recorded at cost and amortized to face value. Short-term investments include certificates of deposit, auction rate certificates, auction rate preferred securities, municipal preferred securities, federal agency issues and mutual funds. The auction rate securities are adjustable-rate securities with dividend rates that are reset periodically by bidders through periodic "Dutch auctions" generally conducted every 7 to 49 days by a trust company or broker/dealer on behalf of the issuer. The Company believes these securities are highly liquid investments through the related auctions; however, the collateralizing securities have stated terms of up to thirty-four (34) years. The investment instruments are rated A or higher by Standard & Poor's Ratings Group, or equivalent. The Company's investments are intended to establish a high-quality portfolio that preserves principal, meets liquidity needs, avoids inappropriate concentrations and delivers an appropriate yield in relationship to the Company's investment guidelines and market conditions. Given the short-term nature of the majority of these investments, and that we have no borrowings outstanding, we are not subject to significant interest rate risk.

LEASE PORTFOLIO. We offer to our customers lease financing and other services, including our TotalSolution program, through our Inter-Tel Leasing subsidiary. We fund these programs in part through the sale to financial institutions of rental payment streams under the leases. Upon the sale of the rental payment streams, we continue to service the leases and maintain limited recourse on the leases. We maintain reserves for loan losses on all leases based on historical loss experience, past due accounts and specific account analysis. Although to date we have been able to resell the rental streams from leases under our lease programs profitably and on a substantially current basis, the timing and profitability of lease resales could impact our business and operating results, particularly in an environment of fluctuating interest rates and economic uncertainty. If we were required to repurchase rental streams and realize losses thereon in amounts exceeding our reserves, our operating results could be materially adversely affected. See "Liquidity and Capital Resources" and "Critical Accounting Policies and Estimates" in Management's Discussion and Analysis for more information regarding our lease portfolio and financing.

IMPACT OF FOREIGN CURRENCY RATE CHANGES. We invoice the customers of our international subsidiaries primarily in the local currencies of our subsidiaries for product and service revenues. Inter-Tel is exposed to foreign exchange rate fluctuations as the financial results of foreign subsidiaries are translated into U.S. dollars in consolidation. The impact of foreign currency rate changes has historically been insignificant.

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### ITEM 4. CONTROLS AND PROCEDURES

*Evaluation of disclosure controls and procedures.* Our management evaluated, with the participation of our Chief Executive Officer and our Chief Financial Officer, the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the "Exchange Act") as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our management, including our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are designed, and are effective to give reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and to ensure that information required to be disclosed in the reports filed or submitted under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, in a manner that allows timely decisions regarding required disclosure.

*Changes in internal controls over financial reporting.* There were no changes in our internal controls over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

### INTER-TEL (DELAWARE), INCORPORATED AND SUBSIDIARIES

### PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

We are involved from time to time in litigation incidental to our business. We believe that the outcome of current litigation will not have a material adverse effect upon our business, results of operations, liquidity or financial condition and will not disrupt our normal operations.

### ITEM 1A. RISK FACTORS

### FORWARD LOOKING STATEMENTS

*This Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. You can identify these statements by the fact that they do not relate strictly to historical or current facts. They use words such as "anticipate", "estimate", "expect", "project", "intend", "plan", "believe" and other words and terms of similar meaning. Any or all of our forward-looking statements in this report and in any other public statements we make may turn out to be wrong. They can be affected by inaccurate assumptions we might make or by known or unknown risks and uncertainties. No forward-looking statement can be guaranteed, and you are cautioned not to place undue reliance on these forward-looking statements. Actual future results may differ materially.*

Except as may be required under the federal securities laws, we undertake no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosures we may make on related subjects in our reports to the SEC. We provide the following cautionary discussion of risks, uncertainties and possibly inaccurate assumptions relative to our business. These are factors that we think could cause our actual results to differ materially from expected and historical results. Other factors besides those listed here could also adversely affect us. This discussion is provided as permitted by the Private Securities Litigation Reform Act of 1995.

Set forth below is a detailed discussion of certain of these risks and other risks affecting our business. The categorization of risks set forth below is meant to help you better understand the risks facing our business and is not intended to limit your consideration of the possible effects of these risks to the listed categories. Any adverse effects related to the risks discussed below may, and most likely will, affect many aspects of our business.

***Risks Related to Our Business***

**Our operating results have historically depended on a number of factors, and these factors may cause our operating results to fluctuate in the future.**

Our quarterly operating results have historically depended on, and may fluctuate in the future as a result of, many factors including:

- volume and timing of orders received during the quarter;

- gross margin fluctuations associated with the mix of products sold;
- the mix of distribution channels;
- general economic conditions and the condition of the markets our business addresses;
- patterns of capital spending by customers;
- the timing of new product announcements and releases by us and our competitors and other competitive factors;
- pricing pressures;
- the cost and effects of acquisitions;

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- the availability and cost of products and components from our suppliers, including shipping and manufacturing problems associated with subcontracted vendors;
- the impact on our business of the E-Rate settlement, the one year debarment of Inter-Tel Technologies from E-Rate opportunities by the FCC, and expected fines and penalties associated with the GSA variances and noncompliance which could affect both our government business and our commercial business;
- government business and our commercial business;
- the impact on our business of settlements, continuing litigations, proceedings and other contingencies, which could affect our business;
- the impact on our business of costs and uncertainties resulting from shareholder actions, including actual or potential proxy contests or tender offers;
- the potential impact of accounting pronouncements, such as FIN 48 or FAS 123R;
- national and regional weather patterns; and
- threats of or outbreaks of war, hostilities, terrorist acts or other civil disturbances.

In addition, we have historically operated with a relatively small backlog for new systems sales (excluding our contractual maintenance arrangements and contracts associated with long distance resale activity), with sales and operating results in any quarter depending principally on orders booked and shipped in that quarter. In the past, we have recorded a substantial portion of our net sales for a given quarter in the third month of that quarter, with a concentration of such net sales in the last two weeks of the quarter. Market demand for investment in capital equipment such as business communications systems and associated call processing and voice processing software applications depends largely on general economic conditions and can vary significantly as a result of changing conditions in the economy as a whole, as well as heightened competitive pressures. We cannot assure you that we can continue to be successful operating with a small backlog or whether historical backlog trends will continue in the future.

Our expense levels are based in part on expectations of future sales and, if sales levels do not meet expectations, our operating results could be harmed. In addition, because sales of business communications systems through our dealers, including dealers from our acquired Lake operations, typically produce lower gross margins than sales through our direct sales organization, operating results have varied, and will continue to vary based upon the mix of sales through direct and indirect channels. In addition, in the recent past we have derived a significant part of our revenue from recurring revenue streams, which typically produce higher gross margins. If we do not maintain recurring revenue streams at current or historic levels, our operating results would suffer unless we significantly increased sales to new customers. Moreover, particularly in an environment of fluctuating interest rates, the timing and profitability of lease resales from quarter to quarter could impact operating results. Long distance, DataNet, national, government and education accounts, and our third-party product sales, which typically carry lower gross margins than our core business, have grown in recent periods at a faster rate than our overall net sales, although gross margins may fluctuate in these divisions from period to period. Consolidated gross margins could be harmed if long distance calling services continue to increase as a percentage of net sales or if gross margins from this division decline. We also experience seasonal fluctuations in our operating results, as net sales for the first quarter is frequently less than the fourth quarter, and net sales for the third quarter is frequently less than the second quarter. As a result of these and other factors, we have historically experienced, and could continue to experience in the future, fluctuations in net sales and operating results on a quarterly basis.

**Our market is subject to rapid technological change and to compete successfully, we must continually introduce new and enhanced products and services that achieve broad market acceptance.**

The market for our products and services is characterized by rapid technological change, evolving industry standards and vigorous customer demand for new products, applications and services. To compete successfully, we must continually enhance our existing telecommunications products, related software and customer services, and develop new technologies and applications in a timely and cost-effective manner. If we fail to introduce new products and services that achieve broad market acceptance and on a timely basis, or if we do not adapt our existing products and services to customer demands or

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evolving industry standards, our business could be significantly harmed. Problems and delays associated with new product development have in the past contributed to lost sales. In particular, we believe that the delayed roll-out of the Inter-Tel 5000 Network Communication Platform contributed to lost sales in 2005 and 2006. In addition, current competitors or new market entrants may offer products, applications or services that are better adapted to changing technology or customer demands and that could render our products and services unmarketable or obsolete. This could lead to write-downs of inventory that could be material to our results of operations.

During the first quarter of 2006, Inter-Tel announced the future release of the Inter-Tel 5600 and Inter-Tel 7000 products, both of which address larger IP PBX configurations. The Inter-Tel 5600 was released in June 2006. If the Inter-Tel 7000 is released late or if these products are not commercially accepted, then the company's financial performance would likely be materially and adversely affected.

In addition, if the markets for collaboration applications, Internet Protocol network products, SIP products and applications, or related products fail to develop or continue to develop more slowly than we anticipate, or if we are unable for any reason to capitalize on any of these emerging market opportunities, our business, financial condition and operating results could be significantly harmed.

**Our future success largely depends on increased commercial acceptance of our Inter-Tel 5000 series and Inter-Tel 7000 Network Communications Solutions, the Lake OfficeLink product (branded EncoreCX® in North America), the Lake Sigma product (branded Sprint Connection Central™ in North America), speech recognition, Interactive Voice Response, presence management, collaboration, messaging products, Session Initiation Protocol (SIP) applications, and related computer-telephony products, as well as continued acceptance of our Axxess® systems and software.**

Over the past two years, we have introduced a number of new products and platforms, including: Inter-Tel Audio and Web Conferencing, a SIP-based web and audio conferencing application; Inter-Tel Webconferencing and Inter-Tel Remote support (collaboration) solutions; Model 8500 series digital endpoints; Model 8600 series Multi-protocol SIP endpoints; the Inter-Tel 5000 Network Communications Platform and updates; enhanced convergence features on the Axxess system; integrated web collaboration and video conferencing capabilities into our Unified Communicator® application, and several other telephony-related products. In recent history, sales of our Axxess business communications systems and related software have comprised a substantial portion of our net sales. Our future success depends, in large part, upon increased commercial acceptance and adoption of the products or platforms identified above, including the Inter-Tel 5000 series and Inter-Tel 7000 Network Communications products, the Unified Communicator® products, Contact Center Suite ACD products, web and audio conferencing collaboration technology, the Lake Communications converged systems and software, SIP standards-based applications and devices, new speech recognition and Interactive Voice Response products, and future upgrades and enhancements to these products and networking platforms as well as the continued acceptance of the Axxess systems and software. We cannot assure you that these products or platforms will achieve commercial acceptance in the future.

**We have many competitors and expect new competitors to enter our market, which could increase price competition and spending on research and development and which may impair our ability to compete successfully.**

The markets for our products and services are extremely competitive and we expect competition to increase in the future, particularly as the networking and telephony industries continue to consolidate and the shift to IP-centric enterprise telephony solutions accelerate. Our current and potential competitors in our primary business segments include:

- PABX, converged systems and IP-PBX providers, distributors, or resellers such as Aastra, Adtran, Alcatel, Altigen, Avaya, Cisco Systems, 3Com, Iwatsu, Interactive Intelligence, Lucky Goldstar, Mitel, NEC, Nortel, Panasonic, Samsung, ShoreTel, Siemens, Toshiba, Vertical Networks/ArtiSoft/Comdial and Vodavi;
- large data routing and convergence companies such as 3Com, Adtran and Cisco Systems;
- voice processing applications providers such as ADC, InterVoice-Brite, Active Voice (a subsidiary of NEC America), Avaya, and Captaris (formerly AVT);

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- web collaboration product and service providers, such as Centra, eDial (a division of Alcatel), IBM, Microsoft, Raindance Communications, and WebEx;
- hosting service providers such as Layered Technologies and Vonage using servers to host call processing functions that have traditionally been owned by customers;
- long distance services providers such as AT&T, MCI, Qwest and Sprint;
- large computer and software corporations such as IBM, HP, Intel and Microsoft;
- peer-to-peer softphone services such as Skype/eBay;
- regional Bell operating companies, or RBOCs, competitive local exchange companies, or CLECs; cable television companies, IP Centrex service providers, and satellite and other wireless and wireline broadband service providers offering IP centrex services such as AT&T, Covad, Level-3, Qwest, SBC, and Time-Warner Telecom; and
- independent leasing companies that provide telecom equipment financing.

These and other companies may form strategic relationships with each other to compete with us. These relationships may take the form of strategic investments, joint-marketing agreements, licenses or other contractual arrangements. Strategic relationships and business combinations could increase our competitors' ability to address customer needs with their product and service offerings that are broader than the product and service offerings we provide. In this regard, Microsoft and Nortel have recently announced an alliance presumably designed to offer business communications linked with business applications.

Many of our competitors and potential competitors have substantially greater financial, customer support, technical and marketing resources, larger customer bases, longer operating histories, greater name recognition and more established relationships in the industry than we do. We cannot assure you that we will have the resources or expertise to compete successfully, particularly as the market for IP network voice communications evolves and competitors like Cisco become more prominent in our industry. Compared to us, our competitors may be able to:

- offer broader product and service offerings;
- develop and expand their product and service offerings more quickly;
- offer greater price discounts or make substantial product promotions;
- adapt to new or emerging technologies and changing customer needs faster;
- take advantage of acquisitions and other opportunities more readily;
- negotiate more favorable licensing agreements with vendors;
- devote greater resources to the marketing and sale of their products; and
- address customers' service-related issues more adequately.

Some of our competitors may also be able to provide customers with additional benefits at lower overall costs or to reduce their gross margins aggressively in an effort to increase market share. We cannot assure you that we will be able to match cost reductions by our competitors. In recent periods, due to competitive pressures, we have discounted pricing on our telephone systems and offered promotions and these actions have negatively impacted our revenues, gross margins and operating results. In addition, we believe there is likely to be further consolidation in our markets, which could lead to having even larger and more formidable competition and other forms of competition that could cause our business to suffer.

**Our products are complex and may contain errors or defects that are detected only after their release, which may cause us to incur significant unexpected expenses and lost sales.**

Our telecommunications products and software are highly complex. Although our new products and upgrades are examined and tested prior to release, they can only be fully tested when used by a large customer base. Consequently, our customers have in the past and may in the future discover program errors, or "bugs," or other defects after new products and upgrades have been released. Some of these bugs may result from defects contained in component parts or software from our suppliers or other third parties that are intended to be compatible with our products and over which we have little or no control. Although we have test procedures and quality control standards in place designed to minimize the number of errors and defects in our products, we cannot assure you that our new products and upgrades will be

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free of bugs when released. If we are unable to quickly or successfully correct bugs identified after release, we could experience the following, any of which would harm our business:

- costs associated with the remediation of any problems;
- costs associated with design modifications;
- loss of or delay in revenues;
- loss of customers;
- damage to our reputation;
- failure to achieve market acceptance or loss of market share;
- increased service and warranty costs;
- liabilities to our customers; and
- increased insurance costs.

**The complexity of our products could cause delays in the development and release of new products and services. As a result, customer demand for our products could decline, which could harm our business. Additionally, changes in technology could render current inventories obsolete.**

Due to the complexity of our products and software, we have in the past experienced and expect in the future to experience delays in the development and release of new products or product enhancements. If we fail to introduce new software, products or services in a timely manner, or fail to release upgrades to our existing systems or products and software on a regular and timely basis, customer demand for our products and software could decline, which would harm our business. For instance, we believe that a delay in connection with our release of the Inter-Tel 5000 Network Communications Platform may have unfavorably impacted our sales efforts in 2005 and 2006. Additionally, as technology changes and as we or our competitors release new products, there is a risk that our current products and inventories could become obsolete or excessive leading to write-downs of our inventory balances in amounts that could be material to our results of operations. During Q1 2006, Inter-Tel announced the planned releases of the Inter-Tel 5600 product and the new Inter-Tel 7000 LAN telephony system. The Inter-Tel 5600 released on schedule in June 2006, but if the general availability of the Inter-Tel 7000 is delayed or if these products are not commercially accepted, then Inter-Tel financial results will be impacted.

**Our founder and former Chief Executive Officer controls approximately 19.5% of our Common Stock, may be able to exert significant influence over the Company and has signaled his willingness to engage with the Company with respect to significant matters.**

As of June 30, 2006, Steven G. Mihaylo, a shareholder and member of Inter-Tel's Board of Directors, beneficially owned approximately 19.5% of the existing outstanding shares of the Common Stock of Inter-Tel. As a result, he has the ability to exercise significant influence over all matters requiring shareholder approval. In addition, the concentration of ownership could have the effect of accelerating, delaying or preventing a change in control of Inter-Tel. On February 22, 2006, Mr. Mihaylo resigned as Chief Executive Officer of Inter-Tel, and on March 6, 2006, Mr. Mihaylo resigned as a director of Inter-Tel. In a Form 13D filed by Mr. Mihaylo on March 6, 2006, Mr. Mihaylo stated that he may acquire additional shares of Common Stock or dispose of shares of Common Stock, or may suggest or propose to Inter-Tel's management or Board, or take a position with respect to, an extraordinary corporate transaction, sale or transfer of assets of Inter-Tel, changes in the Board or management of Inter-Tel, changes in the capitalization of Inter-Tel, changes in Inter-Tel's business or corporate structure and/or similar actions and transactions, including without limitation, a proposal to acquire Inter-Tel in a going private transaction, tender offer or similar transaction. In furtherance of such intention, Mr. Mihaylo filed with the SEC proxy soliciting material on April 10, 2006, proposing for election three (3) directors different from the Board's nominees and setting forth numerous other proposals, including specific proposals with regard to governance and anti-takeover matters. Pursuant to a Settlement Agreement entered into between the Company and Mr. Mihaylo on May 5, 2006, and amended on June 28, 2006, the Company agreed to expand the number of directors to eleven (11) and to appoint Mr. Mihaylo's nominees to the Board of Directors in exchange for Mr. Mihaylo's withdrawal of his proposals and proxy solicitation. The Company also agreed to timely review any acquisition proposal offered by Mr. Mihaylo and, should such proposal not be accepted by the Board, to call a special meeting of shareholders to consider Mr. Mihaylo's previously submitted proposals, including the proposal urging the Board to arrange for the prompt sale of the Company (the "Sell the Company Proposal"). The Company will not contest the calling of the special meeting with respect to the Sell the Company Proposal but may contest the meeting for other purposes and the submission of proposals other

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than the Sell the Company Proposal. Subject to our obligations pursuant to the Settlement Agreement, we may oppose the Sell the Company Proposal and any other proposals.

On July 28, 2006, as noted in Steve G. Mihaylo's Form 13D filing, Mr. Mihaylo and Vector Capital Corporation submitted an unsolicited offer to acquire all shares, other than those shares already owned by Mr. Mihaylo, of Inter-Tel Common Stock for $22.50 per share, subject to the negotiation of an agreement and other factors. Pursuant to the terms of the settlement agreement, Inter-Tel's Board of Directors has until August 11, 2006 to respond to the offer. Mr. Mihaylo's recent actions as described above have caused the Company to incur significant legal and other advisory expenses and have subjected the Company and its Board of Directors to shareholder class action litigation. Any future actions that Mr. Mihaylo may take or that the Company may take in response to Mr. Mihaylo's offer may further divert the attention of our Board of Directors and management from the conduct of the Company's business may expose the Company to additional litigation and may cause us to incur additional significant legal, advisory and other expenses.

**Business acquisitions, new business ventures, dispositions or joint ventures entail numerous risks and may disrupt our business, dilute shareholder value and distract management attention.**

As part of our business strategy, we consider acquisitions of, or significant investments in, businesses that offer products, services and technologies complementary to ours. Such acquisitions could materially adversely affect our operating results and/or the price of our common stock. Acquisitions also entail numerous risks, some of which we have experienced and may continue to experience, including:

- unanticipated costs and liabilities;
- difficulty of assimilating the operations, products and personnel of the acquired business;
- difficulties in managing the financial and strategic position of acquired or developed products, services and technologies;
- difficulties in maintaining customer relationships;
- difficulties in servicing and maintaining acquired products, in particular where a substantial portion of the target's sales were derived from our competitor's products and services;
- difficulty of assimilating the vendors and independent contractors of the acquired business;
- the diversion of management's attention from the core business;
- inability to maintain uniform standards, controls, policies and procedures; and
- impairment of relationships with acquired employees and customers occurring as a result of integration of the acquired business.

In March 2005, we acquired all of the outstanding stock of several related entities in Ireland. These entities are similar in nature to our wholesale operations and also include significant technology-related assets. Acquisitions are subject to risks and uncertainties including, but not limited to, those indicated above.

Finally, to the extent that shares of our stock or the rights to purchase stock are issued in connection with any future acquisitions, dilution to our existing shareholders would result and our earnings per share may suffer. Any future acquisitions may not generate additional revenue or provide any benefit to our business, and we may not achieve a satisfactory return on our investment in any acquired businesses.

**We may not be able to adequately protect our proprietary technology and may be infringing upon third-party intellectual property rights.**

Our success depends upon the protection of our proprietary technology. As of June 30, 2006, we held 40 U.S. issued patents and issued patents in several foreign countries for telecommunication and

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messaging products, systems and processes. There are 19 pending U.S. patent applications and several pending foreign patent applications that may mature to enforceable patents. We also rely on copyright, trademark and trade secret laws as well as contractual provisions to protect our intellectual property. Despite these precautions, third parties could copy or otherwise obtain and use our technology without authorization, or independently develop similar technology.

Any patent, trademark or copyright that we own or have applied for is subject to being invalidated, circumvented or challenged by a third party. Effective protection of intellectual property rights may be unavailable or limited in foreign countries. The telecommunications and networking industries are heavily patented, and we cannot assure that the protection of our proprietary rights will be adequate or that competitors will not independently develop similar technology, duplicate our services, or design around any patents or other intellectual property rights we hold. Litigation may be necessary in the future to enforce our intellectual property rights, to protect our trade secrets, to determine the validity and scope of the proprietary rights of others, or to defend against claims of infringement or invalidity. Litigation could be costly, absorb significant management time and harm our business.

Many of our competitors have large patent portfolios, and we are or could become subject to third-party claims that our current or future products or services infringe upon the rights of others. For example, we are subject to claims initiated by Avaya and Lucent, two of our primary competitors, alleging that certain of our key products infringe upon their intellectual property rights, including patents, trademarks, copyrights, or other intellectual property rights. We have viewed presentations from Avaya and Lucent alleging that our Axxess business communications system, associated applications and related 3rd party products that we distribute utilize inventions covered by certain of their patents. We have also made claims against Avaya for infringement of our patents. We are continuing the process of investigating these matters. The ultimate outcomes by their nature are uncertain, and we cannot ensure that these matters, individually or collectively, would not have a material adverse impact on our financial position, liquidity and future results of operations.

When any such claims are asserted against us, among other means to resolve the dispute, we may seek to license the third party's intellectual property rights. Purchasing such licenses can be expensive, and we cannot ensure that a license will be available on prices or other terms acceptable to us, if at all. Alternatively, we could resort to litigation to challenge such a claim. Litigation could require us to expend significant sums of cash and divert our management's attention. In the event a court renders an enforceable decision with respect to our intellectual property, we may be required to pay significant damages, develop non-infringing technology, or acquire licenses to the technology subject to the alleged infringement. Any of these actions or outcomes could harm our business. If we are unable or choose not to license technology, or decide not to challenge a third-party's rights, we could encounter substantial and costly delays in product introductions. These delays could result from efforts to design around asserted third-party rights or our discovery that the development, manufacture or sale of products requiring these licenses could be foreclosed.

**Our reliance on a limited number of suppliers for key components and our dependence on contract manufacturers could impair our ability to manufacture and deliver our products and services in a timely and cost-effective manner.**

We currently obtain certain key components for our communication platforms, including certain microprocessors, integrated circuits, power supplies, voice processing interface cards and IP telephony cards, from a limited number of suppliers and manufacturers. Our reliance on these limited suppliers and contract manufacturers involves risks and uncertainties, including the possibility of a shortage or delivery delay for some key components, quality assurance and costs. We currently manufacture our products, including products manufactured for Lake, through third-party subcontractors located in the United States, Mexico, the People's Republic of China and the United Kingdom. Jabil Circuit, Inc. currently manufactures a significant portion of our products at its Tempe, Arizona, facility, including substantially all of the printed circuit boards used in the Axxess systems and Inter-Tel 5000 series systems. Foreign manufacturing facilities are subject to changes in governmental policies, imposition of tariffs and import restrictions and other factors beyond our control. We have experienced occasional delays in the supply of components and finished goods that have harmed our business. If inventory levels are not adequately maintained and managed we are at risk of not having the appropriate inventory quantities on hand to meet sales demand. We may experience similar delays in the future.

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Our reliance on third party manufacturers and OEM partners involves a number of additional risks, including reduced control over delivery schedules, quality assurance and costs. Our business may be harmed by any delay in delivery or any shortage of supply of components or finished goods from a supplier caused by any number of factors, including but not limited to the acquisition of the vendor by another company. Our business may also be harmed if we are unable to develop alternative or additional supply sources as necessary. To date, we have been able to obtain supplies of components and products in a timely manner even though we do not have long-term supply contracts with any of our contract manufacturers. However, we cannot assure you we will be able to continue to obtain components or finished goods in sufficient quantities or quality or on favorable pricing or delivery terms in the future.

**We derive a substantial portion of our net sales from our dealer network and if these dealers do not effectively promote and sell our products, our business and operating results could be harmed.**

We derive a substantial portion of our net sales through our network of independent dealers. We face intense competition from other telephone, voice processing, and voice and data router system manufacturers for these dealers' business, as most of our dealers carry other products that compete with our products. Our dealers may choose to promote the products of our competitors to our detriment. We have developed programs and offered incentives to our dealers to promote our products, and we cannot assure you that these techniques will continue to be successful. The loss of any significant dealer or group of dealers, or any event or condition harming our dealer network, could harm our business, financial condition and operating results.

**We have been the subject of government investigations, which have resulted in convictions and civil penalties and may cause further competitive and financial harm to our business.**

On January 5, 2005, the Company received court approval of a civil settlement agreement (the "Civil Settlement") and a criminal plea agreement (the "Plea Agreement") with the United States of America, each dated as of December 8, 2004 and disclosed on that same date. The court approval of the Civil Settlement and Plea Agreement resolved the investigation of the Department of Justice into the participation of Inter-Tel Technologies, Inc., the Company's wholly-owned subsidiary ("Technologies"), in a federally administered "E-Rate program" to connect schools and libraries to the Internet. In connection with the Civil Settlement, Technologies paid a penalty of $6.7 million and forgave the collection of certain accounts receivable of $0.3 million related to Technologies' participation in the E-Rate program. In connection with the Plea Agreement, Technologies entered guilty pleas to charges of mail fraud and an antitrust violation. Under the Plea Agreement, Technologies paid a fine of $1.7 million and is observing a three-year probationary period, which has, among other things, required Technologies to implement a comprehensive corporate compliance program. On December 20, 2005, in connection with the Civil Settlement, Technologies paid outside counsel for the plaintiffs in that action $0.1 million in settlement of their demand for attorney's fees and costs. On March 10, 2006, Technologies agreed to pay an additional $0.4 million to plaintiffs' inside counsel in settlement of their separate demand for fees and costs.

Inter-Tel recorded approximately $9.5 million in costs through 2005, including criminal fines, civil settlement and restitution, uncompensated E-Rate work, accounts receivable forgiveness, and related attorneys' fees and other expenses. The payments constituting the primary components of the settlement are not tax deductible. The effect of the resolution was recorded in 2004, although the Company has continued to incur additional legal expenses in connection with the defense of a former employee in connection with this matter pursuant to California statute.

In addition, on January 21, 2005, Inter-Tel Technologies received notification from the Federal Communications Commission (the "FCC") that the Technologies subsidiary was temporarily suspended from participation in the E-Rate program pending a final hearing to determine a possible debarment of three (3) years or more. Technologies contested the scope and length of the proposed debarment from the E-Rate program. The Company was notified on June 30, 2006 that on or about June 21, 2006, the FCC issued its final decision on the matter and imposed upon the Technologies subsidiary a debarment from the E-Rate program of one (1) year from June 30, 2006. Reasons for the shorter period were, among other factors, that Technologies had instituted a compliance program and been cooperative in the investigation and ongoing hearings with the Department of Justice. The FCC order further clarified that the

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parent and other subsidiaries were not debarred. The Company recorded no revenues since January 21, 2005 relating to Inter-Tel Technologies' participation in the E-Rate program.

The existence and disclosure of the Civil Settlement, Plea Agreement and FCC Notice may have already caused competitive harm to Inter-Tel, and these matters may further harm Inter-Tel's business.

During the second quarter of 2005, we identified variances in our sales processes as they relate to certain terms included in the U.S. General Services Administration (GSA) pricing and trade agreement requirements applicable to our business. As a result of this identification, Inter-Tel made voluntary self-disclosure of the matter to the Inspector General of the GSA. The potential variances relate primarily to noncompliance with certain pricing thresholds and noncompliance with trade agreements that are applicable to transactions with certain government agencies. We continue to monitor our compliance and have taken appropriate corrective measures with respect to these potential variances. In the second quarter of 2005, we accrued $1.8 million in estimated pre-tax adjustments, including reductions in net sales and increases to costs, fines and penalties that may be incurred to correct this issue, of which we have paid $1.2 million through June 30, 2006. Our estimate at June 30, 2006 remains the same as the total identified as of the end of the second quarter of 2005. The total sales potentially subject to the GSA agreements were approximately $5.5 million during the period from March 28, 2001 through June 10, 2005. Our current contract with the GSA expires in August 2006, and we have requested and expect to receive an extension of that contract. However, there can be no assurance that the GSA will extend the current agreement or accept a revised agreement.

**We have been involved in legal disputes, which have resulted in a jury verdict, legal settlement and associated legal costs, which may cause further competitive and financial harm to our business.**

During the quarter ended September 30, 2005, pre-tax costs associated with a legal judgment, legal settlement and related costs identified separately in the consolidated statements of income totaled $10.4 million ($0.26 per diluted share after taxes), net of amounts previously accrued. As disclosed in August 2005 on Form 8-K filed with the SEC, a Florida state court jury rendered a verdict against Inter-Tel ("the Florida trial") with respect to a certain commercial dispute with a prior Executone dealer and in the net amount of approximately $7.4 million. The Company also accrued additional legal costs in connection with the Florida trial. Although the Company is appealing the verdict, the Company has accrued the net verdict amount, plus legal costs incurred in the third quarter. Should the Company be successful or unsuccessful in the appeals process, these costs may be adjusted in the future. In connection with the appeal of the Florida trial, the Company posted collateral of $6.3 million in order to secure an appellate bond. The Company also reached a separate settlement in another legal matter during the third quarter in connection with a longstanding dispute with a third-party vendor and customer. The net settlement plus related legal fees incurred during the third quarter for both events totaled approximately $3.0 million, net of amounts previously accrued, and are included in the pre-tax total costs of $10.4 million identified above. Further, in March 2006, other prior Executone dealers filed a complaint in Columbus, Ohio similar to the complaint in the Florida trial. The Company is in the process of evaluating the complaint and conducting initial discovery. Any such similar litigation will subject Inter-Tel to additional expenses and could have an adverse effect on our operating results.

Subsequent to December 31, 2005, the Company settled another legal matter in connection with a longstanding dispute with a former international dealer that existed as of December 31, 2005. The Company recorded an accrual for the settlement amount and related fourth quarter legal fees as of December 31, 2005. The settlement plus related fourth quarter legal fees totaled $1.6 million. Additional legal fees totaling approximately $1.3 million were recorded as period costs during the first quarter of 2006 relating to this matter.

On June 16, 2006, a shareholder class action suit was brought against Inter-Tel and selected Board members in Delaware state court. On June 16 and June 20, 2006, respectively, two additional shareholder class actions against the Company and each of its Board members were filed in Arizona state court. The Delaware action, as amended July 14, 2006, raises claims related to the reincorporation filing by Inter-Tel in Delaware and primarily seeks injunctive relief. The Arizona actions claim breach of fiduciary duty related to the 13D filings by the Company's former CEO. The Company is in the process of evaluating these class action suits.

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Inter-Tel is also subject to litigation in the ordinary course of business. We cannot assure you that any adverse outcome in connection with the litigation described above or ordinary course litigation would not materially impair our business, results of operations, liquidity or financial condition.

**Managing our international sales efforts may expose us to additional business risks, which may result in reduced sales or profitability in our international markets.**

We are currently expending resources to maintain and expand our international dealer network in the countries in which we already have a presence and in new countries and regions. International sales are subject to a number of risks, including changes in foreign government regulations and telecommunication standards, export license requirements, tariffs and taxes, other trade barriers, difficulties in protecting our intellectual property, fluctuations in currency exchange rates, difficulty in collecting receivables, difficulty in staffing and managing foreign operations, and political and economic instability. In particular, the continued hostilities in Iraq and turmoil in the Middle East and North Korea have created an uncertain international economic environment and we cannot predict the impact of these acts, any future terrorist acts or any related military action on our efforts to expand our international sales. Fluctuations in currency exchange rates could cause our products to become relatively more expensive to customers in a particular country, leading to a reduction in sales or profitability in that country. In addition, the costs associated with developing international sales or an international dealer network may not be offset by increased sales in the short term, or at all. Any of these risks could cause our products to become relatively more expensive to customers in a particular country, leading to reduced sales or profitability in that country.

**If we lose key personnel or are unable to hire additional qualified personnel as necessary, we may not be able to achieve our objectives.**

We depend on the continued service of, and our ability to attract and retain, qualified technical, marketing, sales and managerial personnel, many of whom would be difficult to replace. Competition for qualified personnel is intense, and we have historically had difficulty in hiring employees in the timeframe we desire, particularly skilled engineers or sales personnel. The loss of any of our key personnel or our failure to effectively recruit additional key personnel could make it difficult for us to manage our business, complete timely product introductions or meet other critical business objectives. Moreover, our operating results could be impaired if we lose a substantial number of key employees from recent acquisitions, including personnel from acquisitions identified in Note C to the Consolidated Financial Statements. We cannot assure you we will be able to continue to attract and retain the qualified personnel necessary for the development of our business.

**Our IP network products may be vulnerable to viruses, other system failure risks and security concerns, which may result in lost customers or slow commercial acceptance of our IP network products.**

Inter-Tel's IP telephony and network products may be vulnerable to computer viruses or similar disruptive problems. Computer viruses or problems caused by third parties could lead to interruptions, delays or cessation of service that could harm our operations and revenues. In addition, we may lose customers if inappropriate use of the Internet or other IP networks by third parties jeopardizes the security of confidential information, such as credit card or bank account information or the content of conversations over the IP network. In addition, user concerns about privacy and security may cause IP networks in general to grow more slowly, and impair market acceptance of our IP network products in particular, until more comprehensive security technologies are developed and deployed industry-wide.

**We may be unable to achieve or manage our growth effectively, which may harm our business.**

The ability to operate our business in an evolving market requires an effective planning and management process. Our efforts to achieve growth in our business have placed, and are expected to continue to place, a significant strain on our personnel, management information systems, infrastructure and other resources. In addition, our ability to manage any potential future growth effectively will require us to successfully attract, train, motivate and manage new employees, to integrate new employees into our overall operations and to continue to improve our operational, financial and management controls and procedures. Furthermore, we expect we will be required to manage an increasing number of relationships

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with suppliers, manufacturers, customers and other third parties. If we are unable to implement adequate controls or integrate new employees into our business in an efficient and timely manner, our operations could be adversely affected and our growth could be impaired.

**The introduction of new products and services has lengthened our sales cycles, which may result in significant sales and marketing expenses.**

In the past few years, we introduced IP telephony enhancements to the Axxess® system as well as presence management and collaboration applications, which are typically sold to larger customers at a higher average selling price and often represent a significant expenditure in communications infrastructure by the prospective enterprise customer. In addition, the announced Inter-Tel 5600 and the Inter-Tel 7000 products are targeted at larger customers. Accordingly, the purchase of our products typically involves numerous internal approvals relating to the evaluation, testing, implementation and acceptance of new technologies. This evaluation process frequently results in a lengthy sales process, which can range from a few months to more than 12 months, thereby subjecting our sales cycle to a number of significant uncertainties concerning budgetary constraints and internal acceptance reviews. The length of our sales cycle also may vary substantially from customer to customer and along product lines. While our customers are evaluating our products before placing an order with us, we may incur substantial sales and marketing expenses and expend significant management effort. In addition, installation of multiple systems for large, multi-site customers may occur over an extended period of time, and depending on the contract terms with these customers, revenues may be recognized over more than one quarter, as systems are completed in separate phases and accepted by the customers. Consequently, if sales forecasted from such customers for a particular quarter are not realized in that quarter, our operating results could be materially adversely affected.

**We rely heavily upon third-party packaged software systems to manage and run our business processes, to provide certain products and services and to produce our financial statements. From time to time we upgrade these systems to ensure continuation of support and to expand the functionality of the systems to meet our business needs. The risks associated with the upgrade process include disruption of our business processes, which could harm our business.**

We currently run third-party applications for data processing in our distribution center operations, shipping, materials movement, customer service, invoicing, sales functions, financial record keeping and reporting, and for other operations and administrative functions. The nature of the software industry is to upgrade software systems to make architectural changes, increase functionality, improve controls and address software bugs. Over time, older versions of the software become less supported or unsupported by our vendors for financial and other reasons and eventually become obsolete. The primary supplier of our third-party applications provides notice of the dates that the supplier will de-support the software, and companies are expected to either make plans to upgrade to newer versions or operate without their support. While our primary third-party supplier and other third-party vendors may provide advanced notice of product upgrade schedules and take other steps to make the upgrade process as straightforward as possible, we are subject to risks associated with the process, and in some cases we may choose to continue to utilize and maintain the unsupported third-party software using our own information systems personnel. Our software systems could become unstable following an upgrade process and impact our ability to process data properly in these systems, including timely and accurate shipment of products, invoicing our customers properly and the production of accurate and timely financial statements. There are risks associated with failing to apply necessary security upgrades intended to resolve vulnerabilities. While we strive to take necessary precautions and properly test security-related upgrades before applying these upgrades, we must weigh the risks of not applying the upgrade against the risks of vulnerabilities being exploited for malicious purposes by an outside entity. Should a security vulnerability be exploited, our systems could become unstable and/or data could be compromised, thereby adversely affecting our business. We expect to affect software upgrades in the future and cannot assure you these software upgrades or enhancements will operate as intended or be free from bugs or that we will be able to operate effectively using unsupported third-party software using our existing personnel and resources. If we are unable to successfully integrate new software into our information systems, our operations, customer service and financial reporting could be adversely affected and could harm our business.

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**Our stock price has been and may continue to be volatile, impairing your ability to sell your shares at or above purchase price.**

The market price for our common stock has been highly volatile. The volatility of our stock could be subject to continued wide fluctuations in response to many risk factors listed in this section, and others beyond our control, including:

- announcements of developments relating to our business;
- investors' reactions to the proxy contest and/or settlement thereof, as well as the recent proposal by Mr. Mihaylo and Vector Capital Corporation to acquire the company and the corresponding prospective response by Inter-Tel's board of directors to such offer;
- fluctuations in our operating results;
- the impact of our dividend announcements, repurchase program or sales of stock by officers and directors;
- shortfalls in revenue or earnings relative to securities analysts' expectations;
- announcements of technological innovations or new products or enhancements by us or our competitors, including product delays;
- announcements of acquisitions or planned acquisitions of other companies or businesses;
- investors' reactions to acquisition announcements or any forecasts of our future results;
- general economic conditions in the telecommunications industry;
- the market for Internet-related voice and data products and services;
- changes in the national or worldwide economy;
- changes in legislation or regulation affecting the telecommunications industry;
- developments relating to our intellectual property rights and the intellectual property rights of third parties;
- litigation or governmental investigations of our business practices;
- the impact on our business of the E-Rate settlement, the one year debarment of Technologies from the E-Rate program, and expected fines and penalties associated with the GSA variances and noncompliance which could affect both our government business and our commercial business;
- the impact on our business of settlements, continuing litigations, proceedings and other contingencies, which could affect our business;
- changes in our relationships with our customers and suppliers, including shipping and manufacturing problems associated with subcontracted vendors;
- national and regional weather patterns; and
- threats of or outbreaks of war, hostilities, terrorist acts or other civil disturbances.

In addition, stock prices of technology companies in general, and for voice and data communications companies in particular, have experienced extreme price fluctuations in recent years which have often been unrelated to the operating performance of affected companies. We cannot assure you the market price of our common stock will not experience significant fluctuations in the future, including fluctuations unrelated to our performance.

**Changes in stock option accounting rules have adversely impacted our reported operating results prepared in accordance with generally accepted accounting principles, and may affect our stock price and our competitiveness in the employee marketplace.**

Technology companies like ours have a history of using broad-based employee stock option programs to hire, provide incentives for and retain our workforce in a competitive marketplace. Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123") allowed companies the choice of either using a fair value method of accounting for options, which would result in expense recognition for all options granted, or using an intrinsic value method, as prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25), with a pro forma disclosure of the impact on net income (loss) of using the fair value option expense recognition method. We previously elected to apply APB 25 and accordingly, prior to 2006, we generally did not recognize any expense with respect to employee stock options as long as such options are granted at exercise prices equal to the fair value of our Common Stock on the date of grant.

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In December 2004, the FASB issued Statement No. 123 (revised 2004), Share-Based Payment ("SFAS 123R"), which replaced SFAS No. 123, Accounting for Stock-Based Compensation, (SFAS 123) and superseded APB Opinion No. 25, Accounting for Stock Issued to Employees. SFAS 123R requires all share-based payments to employees, including grants of employee stock options, performance shares, and employee stock purchase plan shares, to be recognized in the financial statements over the period during which employees are required to provide services based on their grant-date fair values. The pro forma disclosures previously permitted under SFAS 123 are no longer an alternative to financial statement recognition. We adopted SFAS No. 123R using the modified prospective application method as defined by SFAS No. 123R and accordingly began recognizing compensation expense for all unvested and partially vested stock options, employee stock purchase plan shares in the first quarter of 2006. SFAS 123R has had a material impact on our consolidated results of operations and earnings per share. This new statement could impact our ability to utilize broad-based employee stock plans to reward employees and could result in a competitive disadvantage to us in the employee marketplace.

***Risks Related to Our Industry***

**Reductions in spending on enterprise communications equipment may materially and adversely affect our business.**

The overall economic conditions of the last several years have had and may continue to have a harmful effect on the market for enterprise communications equipment. Our customers have reduced significantly their capital spending on communications equipment in an effort to reduce their own costs and bolster their revenues. The market for enterprise communications equipment may only grow at a modest rate or possibly not grow at all, and our financial performance has been and may continue to be materially and adversely affected by the reductions in spending on enterprise communications equipment.

**The emerging market for IP network telephony is subject to market risks and uncertainties that could cause significant delays and expenses.**

Although the IP network voice communication market is reaching mainstream, it is still developing, is evolving rapidly and is characterized by an increasing number of market entrants who have introduced or developed products and services for Internet or other IP network voice communications. As is typical of a new and rapidly evolving industry, the demand for and market acceptance of, recently introduced IP network products and services are highly uncertain. We cannot assure you that IP voice networks will not change and shift as the market develops. Even if IP voice markets fully develop, we cannot assure that our products, including the IP telephony features of the *Axxess* systems, the Inter-Tel 5000 Network Communication Solutions, the upcoming Inter-Tel 7000 Network Communication Solutions, our SIP/IP endpoints and IP applications will successfully compete against other market players and attain broad market acceptance.

Moreover, the adoption of IP voice networks and importance of development of products using industry standards such as SIP, generally require the acceptance of a new way of exchanging information. In particular, enterprises that have already invested substantial resources in other means of communicating information may be reluctant or slow to adopt a new approach to communications. If the market for SIP network voice communications fails to develop or develops more slowly than we anticipate, our SIP network telephony products such as the Inter-Tel 7000 could fail to achieve market acceptance, which in turn could significantly harm our business, financial condition and operating results. This growth may be inhibited by a number of factors, such as quality of infrastructure; security concerns; equipment, software or other technology failures; regulatory encroachments; inconsistent quality of service; poor voice quality over IP networks as compared to circuit-switched networks; and lack of availability of cost-effective, high-speed network capacity. Moreover, as IP-based data communications and telephony usage grow, the infrastructure used to support these IP networks, whether public or private, may not be able to support the demands placed on them and their performance or reliability may decline. The technology that allows voice and facsimile communications over the Internet and other data networks, and the delivery of other value-added services, is still in the early stages of development.

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**Government regulation of third party long distance and network service entities on which we rely may harm our business.**

Our supply of telecommunications services and information depends on several long distance carriers, RBOCs, local exchange carriers, or LECs, and competitive local exchange carriers, or CLECs. We rely on these carriers to provide local and long distance services, including voice and data circuits, to our customers and to provide us with billing information. Long distance services are subject to extensive and uncertain governmental regulation on both the federal and state level. We cannot assure you that the increase in regulations will not harm our business. Our current contracts for the resale of services through long distance carriers include multi-year periods during which we have minimum use requirements and/or costs. The market for long distance services is experiencing, and is expected to continue to experience significant price competition, and this may cause a decrease in end-user rates. We cannot assure you that we will meet minimum use commitments, that we will be able to negotiate lower rates with carriers if end-user rates decrease or that we will be able to extend our contracts with carriers at favorable prices. If we are unable to secure reliable Network Services from certain long distance carriers, RBOCs, LECs and CLECs, or if these entities are unwilling or unable to provide telecommunications services and billing information to us on favorable terms, our ability to expand our own Network Services will be harmed. Carriers that provide telecommunications services to us may also experience financial difficulties, up to and including bankruptcies, which could harm our ability to offer telecommunications services.

**Consolidation within the telecommunications industry could increase competition and adversely affect our business.**

There has been a trend in the telecommunications industry toward consolidation and we expect this trend to continue as the industry evolves. As a result of this consolidation trend, new stronger companies may emerge that have improved financial resources, enhanced research and development capabilities and a larger and more diverse customer base. The changes within the telecommunications industry may adversely affect our business, operating results and financial condition.

**Terrorist activities and resulting military and other actions could harm our business.**

Terrorist attacks in New York and Washington, D.C. in September of 2001 disrupted commerce throughout the world. The continued threat of terrorism, the conflict in Iraq and the potential for additional military action and heightened security measures in response to these threats may continue to cause significant disruption to commerce throughout the world. To the extent that disruptions result in a general decrease in corporate spending on information technology or advertising, our business and results of operations could be harmed. We are unable to predict whether the conflict in Iraq and its aftermath, the threat of terrorism or the responses thereto will result in any long-term commercial disruptions or if such activities or responses will have a long-term adverse effect on our business, results of operations or financial condition. Additionally, if any future terrorist attacks were to affect the operation of the Internet or key data centers, our business could be harmed. These and other developments arising out of the potential attacks may make the occurrence of one or more of the factors discussed herein more likely to occur.

**We Are Exposed To Costs And Risks Associated With Compliance With Changing Laws, Regulations And Standards In General, and Specifically With Regulation Of Corporate Governance And Disclosure Standards.**

We are spending a substantial amount of management time and external resources to comply with existing and changing laws, regulations and standards in general, and specifically relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, new SEC regulations, PCAOB and Nasdaq Stock Market rules, as well as commercial dealings with other government entities. In particular, Section 404 of the Sarbanes-Oxley Act of 2002 requires management's annual review and evaluation of our internal control systems, and attestations of the effectiveness of these systems by our management and by our independent auditors. We completed our documentation and testing of our internal control systems and procedures as required for 2004 and 2005, and are working our plan for 2006. This process has required us to hire additional personnel and use outside advisory services and resulted in additional accounting and legal expenses. The results of the documentation and testing for 2004 and 2005 indicated that we had adequate internal controls over financial reporting. However, if in the

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future our chief executive officer, chief financial officer or independent auditors determine that our controls over financial reporting are not effective as defined under Section 404, investor perceptions of Inter-Tel may be adversely affected and could cause a decline in the market price or our stock. Failure to comply with other existing and changing laws, regulations and standards could also adversely affect the Company.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

*Board Authorization to Repurchase up to $75 Million of Inter-Tel Stock.* On February 15, 2005, Inter-Tel announced that its Board of Directors approved a stock repurchase program, with no stated expiration date, in which Inter-Tel may purchase up to $75 million of its Common Stock in the open market from time to time, depending upon general market conditions, the Company's share price, the level of employee stock option exercises, the level of employee stock purchase plan purchases, the availability of funds and other factors. The Company repurchased 716,500 shares of its Common Stock pursuant to the Plan during the year ended December 31, 2005, but the Company did not repurchase any shares of its Common Stock during the first six months of 2006.

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### ISSUER PURCHASES OF EQUITY SECURITIES

| Period | (a) Total Number of Shares (or Units) Purchased | (b) Average Price Paid per Share (or Unit) | (c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs | (d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| **2005** | | | | |
| April 1 to April 30 | None | N/A | None | |
| May 1 to May 31 | 716,500 | $19.228 | 716,500 | |
| June 1 to June 30 | None | N/A | None | |
| **2006** | None | N/A | None | |
| Total | 716,500 | $19.228 | 716,500 | $61,223,000(1) |

(1) On February 15, 2005, the Board of Directors approved and the Company announced a plan to repurchase up to $75 million of the common stock of the Company.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES** — Not Applicable

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

Our Annual Meeting of Shareholders was held May 31, 2006 (the Annual Meeting). On March 17, 2006 we mailed a Proxy Statement, pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended, to our shareholders to solicit their votes regarding the following matters that were discussed and approved by our shareholders at our Annual Meeting:

1. Election of Directors: J. Robert Anderson, Alexander L. Cappello, Jerry W. Chapman, Gary D. Edens, Steven E. Karol, Steven G. Mihaylo, Dr. Anil K. Puri, Robert Rodin, Norman Stout, Kenneth L. Urish and Agnieszka Winkler were elected to serve as directors until the 2007 Annual Meeting of Shareholders. The votes were as follows:

| Nominee | For: | Against: | Abstain: |
|---|---|---|---|
| J. Robert Anderson | 19,365,302 | 972,877 | 541,556 |
| Alexander L. Cappello | 19,752,698 | 585,481 | 541,556 |
| Jerry W. Chapman | 11,337,241 | 10,720,210 | 541,556 |
| Gary D. Edens | 19,652,843 | 685,336 | 541,556 |
| Steven E. Karol | 19,783,560 | 554,619 | 541,556 |
| Steven G. Mihaylo | 19,542,220 | 795,959 | 541,556 |
| Dr. Anil K. Puri | 19,672,791 | 665,388 | 541,556 |
| Robert Rodin | 19,403,979 | 934,200 | 541,556 |
| Norman Stout | 19,648,037 | 690,142 | 541,556 |
| Kenneth L. Urish | 19,672,575 | 665,604 | 541,556 |
| Agnieszka Winkler | 19,385,350 | 952,829 | 541,556 |

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2. The shareholders voted on and approved a proposal to change the Company's state of incorporation from Arizona to Delaware (the "Reincorporation"). The votes were as follows:

| | For: | Against: | Abstain: |
|---|---|---|---|
| Proposal to change the Company's state of incorporation | 17,957,389 | 3,109,293 | 22,277 |

3. The shareholders voted on and approved a proposal to approve a special resolution authorizing the Company's Board of Directors to effect an amendment to the Company's Charter Documents requiring the approval of a majority of disinterested shareholders to effect certain business combination transactions involving interested parties. The votes were as follows:

| | For: | Against: | Abstain: |
|---|---|---|---|
| Proposal to approve a special resolution | 18,785,864 | 2,265,078 | 38,017 |

4. The shareholders voted on and approved a proposal to ratify the appointment of Ernst & Young LLP to act as the independent auditors to audit our and our subsidiaries' financial statements for the year 2006. The votes were as follows:

| | For: | Against: | Abstain: |
|---|---|---|---|
| Proposal to ratify the appointment of independent auditors | 20,821,891 | 263,715 | 3,353 |

On May 5, 2006, Inter-Tel entered into a Settlement Agreement with Mr. Steven G. Mihaylo ("Mr. Mihaylo") and Summit Growth Management LLC, a wholly owned affiliate of Mr. Mihaylo ("Summit"), as well as an amendment to the Settlement Agreement on June 28, 2006. The Settlement Agreement, in addition to other related issues, provides for the appointment and nomination of certain individuals to the Board of Directors, the withdrawal of Mr. Mihaylo's proposals and proxy solicitation materials for the 2006 Annual Meeting of Shareholders, and established guidelines for a possible all-cash acquisition proposal. For the six months ended June 30, 2006, total costs for dealing with the proxy solicitation and settlement issues totals approximately $2.0 million. For more details on this Settlement, refer to the Form 8-K filed on May 11, 2006.

**ITEM 5. OTHER INFORMATION** — Not Applicable.

**ITEM 6. EXHIBITS:**

Exhibit 10.66: Form of Performance Share Notice of Grant and Agreement Pursuant to the 1997 Long-Term Incentive Plan

Exhibit 31.1: Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 31.2: Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 32.1: Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

INTER-TEL (DELAWARE), INCORPORATED

| | |
|---|---|
| August 9, 2006 | /s/ Norman Stout<br>Norman Stout<br>Chief Executive Officer |
| August 9, 2006 | /s/ Kurt R. Kneip<br>Kurt R. Kneip<br>Senior Vice President and<br>Chief Financial Officer |

**EXHIBIT "D"**
**BIOGRAPHY INFORMATION**

**Norman Stout**
**Chief Executive Officer**
Mr. Stout was appointed Chief Executive Officer and a member of Inter-Tel's Board of Directors on February 22, 2006. He began his tenure at Inter-Tel in 1994 as a director. Four years later, he joined Inter-Tel as executive vice president, chief administrative officer and president of Inter-Tel Software and Services. Prior to joining Inter-Tel, Mr. Stout was Chief Operating Officer of Oldcastle Architectural Products and since 1996, Mr. Stout also had served as President of Oldcastle Architectural West. Mr. Stout held previous positions as President of Superlite Block; Chief Financial Officer and Chief Executive Officer (successively) of Boorhem-Fields, Inc. of Dallas, Texas; and as a Certified Public Accountant with Coopers & Lybrand. He currently serves on the board of Hypercom Corporation, a public company headquartered in Phoenix, Arizona. Mr. Stout holds a Bachelor of Business Administration degree in Accounting from Texas A&M and an MBA from the University of Texas.

**Craig W. Rauchle**
**President and Chief Operating Officer**
Mr. Rauchle, elected as our President in April of 2005, was previously elected Chief Operating Officer in August 2001 – a title he continues to hold. Mr. Rauchle is responsible for Inter-Tel's sales and sales support functions, marketing, procurement, distribution and research and development activities. He had been our Senior Vice President and continues as President of Inter-Tel Technologies, Inc., our wholly owned sales subsidiary. Mr. Rauchle joined Inter-Tel in 1979 as Branch General Manager of the Denver Direct Sales Office and in 1983 was appointed the Central Region Vice President and subsequently the Western Regional Vice President. From 1990 to 1992, Mr. Rauchle served as President of Inter-Tel Communications, Inc. Mr. Rauchle holds a Bachelor of Arts degree in Communications from the University of Denver.

**Jeff Ford**
**Chief Technology Officer and Division President**
Mr. Ford was elected Senior Vice President in May 1998 and has served as our Chief Technology Officer since 1997. He was elected President of Inter-Tel Integrated Systems, Inc. (IIS) in May 1998, after serving as Senior Vice President of IIS for one year and Vice President of Software Engineering of Inter-Tel Integrated Systems from 1993 to 1997. He joined Inter-Tel in 1983 as a software design engineer. Mr. Ford holds a Bachelor of Science degree in Computer Systems Engineering from Arizona State University and an SEP certificate from the Stanford Graduate School of Business.

**Kurt Kneip**
**Chief Financial Officer**
Mr. Kneip has served as our Chief Financial Officer since September 1993. He has served as Senior Vice President since February 2003 and as Vice President from September 1993 to February 2003. He was elected Secretary and Treasurer in October 1994. In May 1996 he was elected Assistant Treasurer, as John Abbott was elected Treasurer. He joined Inter-Tel in May 1992 as Director of Corporate Tax, after seven years with the accounting firms of Ernst & Young and KPMG Peat Marwick. Mr. Kneip is a Certified Public Accountant, and holds a Bachelor of Science degree in Commercial Economics from South Dakota State University and a Masters Degree in Professional Accountancy from the University of South Dakota.

**Jon Klassen**
**Chief Information Officer**
Mr. Klassen joined Inter-Tel as the chief information officer in 1999. Prior to that, he spent five years as a senior manager at Salt River Project. He also served as Worldcom's director of application development for seven years. Before joining the technology sector, Mr. Klassen worked in the aerospace industry.

He holds a computer science bachelor's degree from Brandon University in Brandon, Manitoba, Canada.

## EXHIBIT "E"
## ILLUSTRATIVE LOCAL EXCHANGE PRICE LIST

LOCAL EXCHANGE SERVICE

**INTER-TEL NETSOLUTIONS, INC.**

REGULATIONS AND SCHEDULE OF INTRASTATE CHARGES
APPLYING TO LOCAL EXCHANGE SERVICE
WITHIN THE STATE OF SOUTH CAROLINA

## CHECK SHEET

The Title Page and pages listed below are inclusive and effective as of the date shown. Original and revised pages as named below contain all changes from the original tariff that are in effect on the date shown on each page.

| Page Number | Revision | Page Number | Revision | Page Number | Revision |
|---|---|---|---|---|---|
| 1 | Original | 41 | Original | 81 | Original |
| 2 | Original | 42 | Original | 82 | Original |
| 3 | Original | 43 | Original | 83 | Original |
| 4 | Original | 44 | Original | 84 | Original |
| 5 | Original | 45 | Original | 85 | Original |
| 6 | Original | 46 | Original | 86 | Original |
| 7 | Original | 47 | Original | 87 | Original |
| 8 | Original | 48 | Original | 88 | Original |
| 9 | Original | 49 | Original | 89 | Original |
| 10 | Original | 50 | Original | 90 | Original |
| 11 | Original | 51 | Original | 91 | Original |
| 12 | Original | 52 | Original | 92 | Original |
| 13 | Original | 53 | Original | 93 | Original |
| 14 | Original | 54 | Original | 94 | Original |
| 15 | Original | 55 | Original | 95 | Original |
| 16 | Original | 56 | Original | 96 | Original |
| 17 | Original | 57 | Original | 97 | Original |
| 18 | Original | 58 | Original | 98 | Original |
| 19 | Original | 59 | Original | 99 | Original |
| 20 | Original | 60 | Original | 100 | Original |
| 21 | Original | 61 | Original | 101 | Original |
| 22 | Original | 62 | Original | 102 | Original |
| 23 | Original | 63 | Original | 103 | Original |
| 24 | Original | 64 | Original | 104 | Original |
| 25 | Original | 65 | Original | 105 | Original |
| 26 | Original | 66 | Original | 106 | Original |
| 27 | Original | 67 | Original | 107 | Original |
| 28 | Original | 68 | Original | 108 | Original |
| 29 | Original | 69 | Original | 109 | Original |
| 30 | Original | 70 | Original | 110 | Original |
| 31 | Original | 71 | Original | 111 | Original |
| 32 | Original | 72 | Original | 112 | Original |
| 33 | Original | 73 | Original | | |
| 34 | Original | 74 | Original | | |
| 35 | Original | 75 | Original | | |
| 36 | Original | 76 | Original | | |
| 37 | Original | 77 | Original | | |
| 38 | Original | 78 | Original | | |
| 39 | Original | 79 | Original | | |
| 40 | Original | 80 | Original | | |



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## EXPLANATION OF SYMBOLS, REFERENCE MARKS, AND ABBREVIATIONS OF TECHNICAL TERMS USED IN THIS TARIFF.

The following symbols shall be used in this tariff for the purpose indicated below:

| | | |
|---|---|---|
| C | - | To signify changed regulation. |
| D | - | To signify discontinued rate or regulation. |
| I | - | To signify increased rate. |
| M | - | To signify a move in the location of text. |
| N | - | To signify new rate or regulation. |
| R | - | To signify reduced rate. |
| S | - | To signify reissued matter. |
| T | - | To signify a change in text but no change in rate or regulation. |



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## APPLICATION OF TARIFF

This tariff sets forth the service offerings, rates, terms and conditions applicable to the furnishing of intrastate communications service by Inter-Tel NetSolutions, Inc. to customers within the local exchange service area, defined herein.



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## SECTION 1 - DEFINITIONS

Certain terms used generally throughout this tariff are defined below.

| | |
|---|---|
| Account Codes: | Allows a User to allocate local calls to a 4-digit, non-verified account code. |
| Advance Payment: | Payment of all or part of a charge required before the start of service. |
| Authorized User: | A person, firm, corporation or other entity that either is authorized by the Customer to use local exchange telephone service or is placed in a position by the Customer, either through acts or omissions, to use local exchange telephone service. |
| Business Service: | A switched network service that provides for dial Station Communications that is described as a business or commercial rate. |
| Call Forward Busy: | Automatically routes incoming calls to a designated answering point when the called line is busy. |
| Call Forward No Answer: | Automatically routes incoming calls to a designated answering point when the called line does not answer within a pre-specified number of rings. |
| Call Forward Variable: | Automatically routes incoming calls to a designated answering point, regardless of whether the user's Station is idle or busy. |
| Call Hold: | Allows the User to hold one call for any length of time provided that neither party goes On Hook. |
| | Allows a User to "park" a call against their directory number within the business group and "unpark" the call from any other directory number. A business group consists of a series of Customer-defined telephone numbers. |



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SECTION 1 - DEFINITIONS (continued)

| | |
|---|---|
| Call Pickup: | Allows a User to answer incoming calls to another Station line within a defined call Pickup group. Call Pickup is provided as either Group Call Pickup, where the predesignated groups can pickup each other's calls by activating an access code or a feature key, or Directed Call Pickup, where any call can be retrieved by dialing a different access code followed by the extension number. |
| Call Waiting: | Provides the User with a burst of tone to indicate that another call is waiting. The second call can either be answered by flashing the switchhook or hanging up the phone and being rung back by the caller. |
| Call Waiting Cancel: | Allows a User to cancel the Call Waiting feature on a per call basis by dialing a specific two-digit code. |
| Call Number Delivery: | Identifies the 10-digit number of the calling party. |
| Call Number Delivery Blocking: | Blocks the delivery of the number to the called party on a per call basis. |
| Class of Service: | Used to prevent a Station from dialing certain codes and numbers. |
| Company: | Inter-Tel NetSolutions, Inc., which is the issuer of this tariff. |
| Commission: | South Carolina Public Service Commission |
| Conference/Six-Way: | The User can sequentially call up to five other people and add them together to make up a six-way call. |



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SECTION 1 - DEFINITIONS (continued)

| | |
|---|---|
| Conference/ Three-Way: | The User can sequentially call up to two other people and add them together to make up a three-way call. |
| Customer: | The person, firm, corporation or other entity that orders service and is responsible for the payment of charges and for compliance with the Company's tariff regulations. |
| Dial Pulse (DP): | The pulse type employed by rotary dial Station sets. |
| Direct Inward Dialing (DID): | A service attribute that routes incoming calls directly to Stations, bypassing a central answering point. |
| Dual Tone Multi-Frequency ("DTMF"): | The pulse type employed by tone dial Station sets. |
| Individual Case Basis: | A service arrangement in which the regulations, rates and charges are developed based on the specific circumstances of the Customer's situation. |
| Joint User: | A person, firm or corporation designated by the Customer as a user of local exchange service furnished to the Customer by the Company, and to whom a portion of the charges for such facilities are billed under a joint use arrangement. |
| LATA: | A local access and transport area established pursuant to the Modification of Final Judgment entered by the United States District Court for the District of Columbia in Civil Action No. 82-0192 for the provision and administration of communications services. |
| Local Calling: | A completed call or telephonic communication between a calling Station and any other Station within the local service area of the calling Station. |



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SECTION 1 - DEFINITIONS (continued)

| | |
|---|---|
| Local Exchange Carrier: | A company that furnishes exchange telephone service. |
| Mbps: | Megabits, or millions of bits, per second. |
| Message Waiting: | This feature provides an indication to a Station User that a message is waiting. Indications may be visual (lamp) or audible (stuttered dialtone). |
| Most Idle Trunk Selection (MIDL): | MIDL Trunk selection occurs when a switching unit selects from a Trunk group the Trunk that has been idle for the longest period of time. |
| Multiple Appearance Directory Numbers: | A directory number that is assigned more than once to one or more Proprietary Business Sets. |
| Multi-Frequency ("MF"): | An inter-machine pulse-type used for signaling between telephone switches, or between telephone switches and PBX/key systems. |
| Non-Recurring Charges: | The one-time initial charges for services or facilities, including but not limited to charges for construction, installation, or special fees, for which the Customer becomes liable at the time the Service Order is executed. |
| Off-Hook: | The term "off-hook" denotes the active condition of a telephone exchange service line. |
| On-Hook: | The term "on-hook" denotes the idle condition of a telephone exchange service line. |



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SECTION 1 - DEFINITIONS (continued)

Presubscription-2 (PIC-2): An arrangement whereby a Customer may select and designate to the Company an Interexchange Carrier it wishes to access, without an access code, for completing intraLATA toll calls. The selected Interexchange Carrier is referred to as the End User's Primary Interexchange Carrier (PIC-2).

Recurring Charges: The monthly charges to the Customer for services, facilities and equipment, which continue for the agreed upon duration of the service.

Residence Service: Residence Service is that service furnished in private homes or apartments, including all parts of the subscriber's domestic establishment, for domestic use and not for substantial occupation use; in the study of a clergyman located in a church, in college fraternity or sorority houses, college dormitories, convents and monasteries for domestic rather than occupational use in residential quarters.

Service Commencement Date: The first day following the date on which the Company notifies the Customer that the requested service or facility is available for use, unless extended by the customer's refusal to accept service which does not conform to standards set forth in the Service Order and this tariff, in which case the Service Commencement Date is the date of the Customer's acceptance of service. The parties may mutually agree on a substitute Service Commencement Date.

Service Order: The written request for local exchange services executed by the Customer and the Company in a format specified by the Company. The signing of a Service Order by the Customer and acceptance thereof by the Company initiates the respective obligations of the parties as set forth therein and pursuant to this tariff, but the duration of the service is calculated from the Service Commencement Date.



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SECTION 1 - DEFINITIONS (continued)

Services: The Company's telecommunications services offered on the Company's network.

Shared Facilities: A facility or equipment system subsystem that can be used simultaneously by several Customers.

Speed Call: Provides a User with the option to call selected directory numbers by dialing a one-two-digit code.

Station: Telephone equipment from or to which calls are placed.

TBD: To Be Determined.

Toll Denial This service blocks access to the Long Distance Message Telecommunications Network, either by direct or operator assistance.

Trunk: A communications path connecting two switching systems in a network, used in the establishment of an end-to-end connection.

User: A customer or any other person authorized by the Customer to use service provided under this tariff.



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# SECTION 2 - REGULATIONS

## 2.1 Undertaking of the Company

### 2.1.1 Scope:

The Company undertakes to furnish communications service in connection with one-way and/or two-way information transmission between points within the State of South Carolina under the terms of this tariff.

The Company is responsible under this tariff only for the services and facilities provided herein, and it assumes no responsibility for any service provided by any other entity that purchases access to the Company network in order to originate or terminate its own services or to communicate with its own customers.

### 2.1.2 Shortage of Equipment or Facilities

The furnishing of service under this tariff is subject to the availability on a continuing basis of all the necessary facilities and is limited to the capacity of the Company's facilities as well as the facilities the Company may obtain from other carriers to furnish service from time to time as required at the sole discretion of the Company.

### 2.1.3 Terms and Conditions

2.1.3.1 Except as otherwise provided herein, service is provided on the basis of a minimum period of at least one month, and shall continue to be provided until canceled by the Customer, via telephone or in writing, on not less than 30 days notice. Unless otherwise specified herein, for the purpose of computing charges in this tariff, a month is considered to have 30 days. All calculations of dates set forth in this tariff shall be based on calendar days, unless otherwise specified herein.



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SECTION 2 – REGULATIONS (continued)

2.1.3.2 Customers may be required to enter into written Service Orders which shall contain or reference the name of the customer, a specific description of the service ordered, the rates to be charged, the duration of the services, and the terms and conditions in this tariff.

2.1.3.3 At the expiration of the initial term specified in each Service Order, or in any extension thereof, service shall continue on a month-to-month basis at the then current rates unless terminated by either party upon 30 days notice. Any termination shall not relieve Customer of its obligation to pay any charges incurred under the Service Order and this tariff prior to termination. The rights and obligations which by their nature extend beyond the termination of the term of the Service Order shall survive such termination.

2.1.3.4 This tariff shall be interpreted and governed by the laws of the State of South Carolina without regard for its choice of laws provision.

2.1.3.5 The Customer has no property right to the Telephone number or any other call number designation associated with services furnished by the Company. The Company reserves the right to change such numbers, or the central office designation associated with such numbers, or both, assigned to the Customer, whenever the Company deems it necessary to do so in the conduct of its business.

2.1.3.6 The Customer agrees to operate Company-provided equipment in accordance with instructions of the Company or the Company's agent. Failure to do so will void Company liability for interruption of service and may make the Customer responsible for damage to equipment pursuant to section 2.1.3.7 below.



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SECTION 2 - REGULATIONS (continued)

2.1.3.7 The Customer agrees to return to the Company all Company-provided equipment delivered to the Customer within five (5) days of the termination of the service in connection with which the equipment was used. Said equipment shall be in the same condition as when delivered to Customer, normal wear and tear only expected. Customer shall reimburse the Company, upon demand, for any costs incurred by the Company due to Customer's failure to comply with this provision.

2.1.4 Liability of the Company

2.1.4.1 The liability of the Company for damages arising out of the furnishing of its Service, including but not limited to mistakes, omissions, interruption, delay, or errors, or other defects, representations, or use of these services or damages arising out of the failure to furnish the service, whether caused by acts or omission, shall be limited to the extension of allowances for interruption as set forth in 2.6, below. The extension of such allowances for interruption shall be the sole remedy of the Customer and the sole liability of the Company. The Company will not be liable for any direct, indirect, incidental, special, consequential, lost profits, exemplary or punitive damages to Customer as a result of any Company service, equipment or facilities, or the acts or omissions or negligence of the Company's employees or agents.



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SECTION 2 - REGULATIONS (continued)

2.1.4.2 The Company's liability for willful misconduct, if established as a result of judicial or administrative proceedings, is not limited by this tariff. The Company's liability, if any, with regard to delayed installation of Company facilities or commencement of service, shall not exceed $1,000. With respect to any other claim or suit, by a Customer or by any others, for damage associated with the ordering (including the reservation of any specific number for use with a service), installation (including delays thereof), provision, termination, maintenance, repair, interruption of restoration of any service or facilities offered under this tariff, and subject to the provisions of Section 2.6, the Company's liability, if any, shall be limited as provided herein.

2.1.4.3 The Company shall not be liable for any delay or failure of performance or equipment due to causes beyond its control, including but not limited to: acts of God, fire, flood, explosion or other catastrophes; and law, order, regulation, direction, action or request of the United States government or of any other government, including state and local governments having or claiming jurisdiction over the Company, or of any department, agency, commission, bureau, corporation or other instrumentality of any one or more of these federal, state, or local governments, or of any military authority; preemption of existing service in compliance with national emergencies; insurrections; riots; wars; unavailability of rights-of-way or materials, or strikes, lockouts, work stoppages, or other labor difficulties.

2.1.4.4 The Company shall not be liable for (a) any act or omission of any entity furnishing the Company or the Company's Customers facilities or equipment used for or with the services the Company offers; or (b) for the acts or omissions of common carriers or warehousemen.



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SECTION 2 - REGULATIONS (continued)

2.1.4.5 The Company shall not be liable for any damages or losses due to the fault of negligence of the Customer or due to the failure or malfunction of Customer-provided equipment or facilities.

2.1.4.6 The Customer shall indemnify and hold the Company harmless from any and all loss, claims, demands, suits, or other action, or any liability whatsoever, whether suffered, made, instituted, or asserted by any other party or person(s), and for any loss, damage, or destruction of any property whether owned by the Customer or others, caused or claimed to have been caused directly or indirectly by the installation, operation; failure to operate, maintenance, removal, condition, location, or use of installation provided by the Company. The Company reserves the right to require each Customer to sign an agreement acknowledging acceptance of the provisions of this section as a condition precedent to such installations.

2.1.4.7 The Company shall not be liable for any defacement of or damage to Customer premises resulting from the furnishing of services or equipment on such premises or the installation or removal thereof, unless such defacement or damage is caused by gross negligence or willful misconduct of the Company's agents or employees. No agents or employees of other participating carriers shall be deemed to be agents or employees of the Company.



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SECTION 2 - REGULATIONS (continued)

2.1.4.8 Notwithstanding the Customer's obligations as set forth in Section 2.3.2, the Company shall be indemnified, defended, and held harmless by the Customer or by others authorized by it to use the service against any claim, loss of damage arising from Customer's use of services furnished under this tariff, including: claims for libel, slander, invasion of privacy or infringement of copyright arising from the material, data, information, or other content transmitted via the Company's service; and patent infringement claims arising from combining or connecting the service offered by the Company with apparatus and systems of the Customer or others. All other claims arising out of any act or omission of the Customer or others, in connection with any service provided by the Company pursuant to this tariff.

2.1.4.9 The entire liability of the Company for any claim, loss, damage or expense from any cause whatsoever shall in no event exceed sums actually paid to the Company by Customer for the specific services giving rise to the claim.

2.1.4.10 The Company makes no warranties or representations, express or implied, including warranties of merchantability or fitness for a particular use, except those expressly set forth herein.

2.1.4.11 The Company shall not be liable for any act or omission of any other company or companies furnishing a portion of the service, or for damages associated with service, channels, or equipment which it does not furnish, or for damages which result from the operation of Customer-provided systems, equipment, facilities or services which are interconnected with Company services.



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SECTION 2 - REGULATIONS (continued)

2.1.4.12 The Company does not guarantee nor make any warranty with respect to service installations at locations at which there is present an atmosphere that is explosive, prone to fire, dangerous or otherwise unsuitable for such installations. The Customer shall indemnify and hold the Company harmless from any and all loss, claims, demands, suits or other action, or any liability whatsoever, whether suffered, made, instituted or asserted by the Customer or by any other party, for any personal injury to, or death of, any person or persons, or for any loss, damage or destruction of any property, whether owned by the Customer or others, caused or claimed to have been caused, directly or indirectly, by the installation, operation, failure to operate, maintenance, removal, presence, condition, locations or use of service furnished by the Company at such locations.



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SECTION 2 - REGULATIONS (continued)

2.1.4.13 The Company shall not be liable for the Customer's failure to fulfill its obligations to take all necessary steps including, without limitation, obtaining, installing and maintaining all necessary equipment, or materials and supplies, for interconnection of the terminal equipment or communications system of the Customer, or any third party acting as its agent, to the Company's network. The Customer shall secure all licenses, permits, rights-of-way, and other arrangements necessary for such interconnection. In addition, the Customer shall ensure that its equipment and/or system or that of its agent is properly interfaced with the Company's service, that the signals emitted into the Company's network are of proper mode, band-with, power, data speed, and signal level for the intended use of the Customer and in compliance with the criteria set forth in Section 2.1.6 following, and that the signals do not damage Company equipment, injure its personnel or degrade service to other Customers. If the Customer or its agent fails to maintain and operate its equipment and/or system or that of its agent properly, with resulting imminent harm to Company equipment, personnel, or the quality of service to other Customers, the Company may, upon written notice, require the use of protective equipment at the Customer's expense. If this fails to produce satisfactory quality and safety, the Company may, upon written notice, terminate the Customer's service without liability.



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SECTION 2 - REGULATIONS (continued)

2.1.4.14 With respect to Emergency Number 911 Service:

(a) This service is offered solely as an aid in handing assistance calls in connection with fire, police and other emergencies. The Company is not responsible for any losses, claims, demands, suits or any liability whatsoever, whether suffered, made, instituted or asserted by the Customer or by any other party or person for any personal injury to or death of any person or persons, and for any loss, damage or destruction of any property, whether owned by the Customer or others, caused or claimed to have been caused by: (1) mistakes, omissions, interruptions, delays, errors or other defects in the provision of this service, or (2) installation, operation, failure to operate, maintenance, removal, presence, condition, location or use of any equipment and facilities furnishing this service.

(b) The Company is not responsible for any infringement or invasion of the right of privacy of any person or persons, caused or claimed to have been caused, directly or indirectly, by the installation, operation, failure to operate, maintenance, removal, presence, condition, occasion or use of emergency 911 service features and the equipment associated therewith, or by any services furnished by the Company including, but not limited to, the identification of the telephone number, address or name associated with the telephone used by the party or parties accessing emergency 911 service, and which arise out of the negligence or other wrongful act of the Company, the Customer, its users, agencies or municipalities, or the employees or agents of any one of them.



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SECTION 2 - REGULATIONS (continued)

2.1.4.15 The Company's liability arising from errors or omissions in Directory Listings, other than charged listing, shall be limited to the amount of actual impairment of the Customer's service and in no event shall exceed one-half the amount of the fixed monthly charges applicable to exchange service affected during the period covered by the directory in which the error or omission occurs. In cases of charged Directory Listings, the liability of the Company shall be limited to an amount not exceeding the amount of charges for the charged listings involved during the period covered by the directory in which the error or omission occurs.

2.1.4.16 In conjunction with a non-published telephone number, as described in Section 3.4.5.3, the Company will not be liable for failure or refusal to complete any call to such telephone when the call is not placed by number. The Company will try to prevent the disclosure of the number of such telephone, but will not be liable should such number be divulged.

2.1.4.17 When a Customer with a non-published telephone number, as defined herein, places a call to the Emergency 911 Service, the Company will release the name and address of the calling party, where such information can be determined, to the appropriate local governmental authority responsible for the Emergency 911 Service, upon request of such governmental authority. By subscribing to service under this tariff Customer acknowledges and agrees with the release of information as described above.

2.1.4.18 In conjunction with the Busy Line Verification and Interrupt Service as described in Section 3.3.2, the Customer shall indemnify and save the Company harmless against all claims that may arise from either party to the interrupted call or any person.



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SECTION 2 - REGULATIONS (continued)

2.1.4.19 The Company shall not be liable for any act or omission concerning the implementation of Presubscription, as defined herein.

2.1.5 Notification of Service-Affecting Activities

The Company will provide the Customer reasonable notification of service-affecting activities that may occur in normal operation of its business. Such activities may include, but are not limited to, equipment or facilities additions, removals or rearrangements and routine preventive maintenance. Generally, such activities are not specific to any individual Customer but affect many Customers services. No specific advance notification period is applicable to all service activities. The Company will work cooperatively with the Customer to determine the reasonable, notification requirements. With some emergency or unplanned service-affecting conditions, such as an outage resulting from cable damage, notification to the Customer may not be possible.



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SECTION 2 - REGULATIONS (continued)

2.1.6 Provisions of Equipment and Facilities

2.1.6.1 The Company shall use reasonable efforts to make available services to a Customer on or before a particular date, subject to the provisions of and compliance by the Customer with the regulations contained in this tariff. The Company does not guarantee availability by any such date and shall not be liable for any delays in commencing service to a Customer.

2.1.6.2 The Company shall use reasonable efforts to maintain facilities and equipment that it furnishes to the Customer. The Customer may not, nor may Customer permit others to, rearrange, disconnect, remove, attempt to repair or otherwise interfere with any of the facilities or equipment installed by the Company, except upon the written consent of the Company.

2.1.6.3 Equipment the Company provided or installs at the Customer Premises for use in connection with the services the Company offers shall not be used for any purpose other than that for which the Company has provided it.

2.1.6.4 The Company shall not be responsible for the installation, operation, or maintenance of any Customer provided communications equipment. Where such equipment is connected to the facilities furnished pursuant to this tariff, the responsibility of the Company shall be limited to the furnishing of facilities offered under this tariff and to the maintenance and operation of such facilities. Beyond this responsibility, the Company shall not be responsible for:



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SECTION 2 - REGULATIONS (continued)

(a) the transmission of signals by Customer provided equipment or for the quality of, or defects in, such transmission; or
(b) the reception of signals by Customer provided equipment; or
(c) network control signaling where such signaling is performed by Customer-provided network control signaling equipment.

2.1.7 Non-routine Installation
At the Customer's request, installation and/or maintenance may be performed outside the Company's regular business hours or in unusual locations. In such cases, charges based on cost of the actual labor, material, or other costs incurred by or charged to the Company will apply. If installation is started during regular business hours but, at the Customer's request, extends beyond regular business hours into time periods including, but not limited to, weekends, holidays, and/or night hours, additional charges may apply.

2.1.8 Ownership of Facilities
Title to all facilities provided in accordance with this tariff remains in the Company, its agents or contractors.

2.2 Prohibited Uses

2.2.1 The services the Company offers shall not be used for any unlawful purpose or for any use as to which the Customer has not obtained all required governmental approvals, authorizations, licenses, consents and permits.

2.2.2 The Company may require a Customer to immediately shut down its transmission of signals if said transmission is causing interference to others.



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SECTION 2 - REGULATIONS (continued)

2.3 Obligations of the Customer

2.3.1 The Customer shall be responsible for:

(a) the payment of all applicable charges pursuant to this tariff;

(b) reimbursing the Company for damage to, or loss of, the Company's facilities or equipment caused by the acts or omissions of the Customer; or the noncompliance by the Customer, with these regulations; or by fire or theft or other casualty on the Customer's premises, unless caused by the negligence or willful misconduct of the employees or agents of the Company. The Company will, upon reimbursement for damages, cooperate with the Customer in prosecuting a claim against the person causing such damage and the Customer shall be subrogated to the Company's right of recovery of damages to the extent of such payment.

(c) providing at no charge, as specified from time to time by the Company, any needed personnel, equipment, space, and power to operate Company facilities and equipment installed on the premises of the Customer, at the level of heating and air conditioning necessary to maintain the proper operating environment of such premises.



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SECTION 2 - REGULATIONS (continued)

2.3 Obligations of the Customer (continued)

2.3.1 The Customer shall be responsible for: (continued)

(d) obtaining, maintaining, and otherwise having full responsibility for all rights-of-way and conduit necessary for installation of fiber optic cable and associated equipment used to provide Local Exchange Service to the Customer from the cable building entrance or property line to the location of the equipment space described in 2.3.1(c). Any costs associated with obtaining and maintaining the rights-of-way described herein, including the costs of altering the structure to permit installation of the Company-provided facilities, shall be born entirely by, or may be charged by the Company to, the Customer. The Company may require the Customer to demonstrate its compliance with this section prior to accepting any order for service;

(e) providing a safe place to work and complying with all laws and regulations regarding the working conditions on the premises at which Company employees and agents shall be installing or maintaining the Company's facilities and equipment. The Customer may be required to install and maintain Company facilities and equipment within a hazardous area if, in the Company's opinion, injury or damage to the Company's employees or property might result from installation or maintenance by the Company. The Customer shall be responsible for identifying, monitoring, removing, and disposing of any hazardous material (e.g. friable asbestos) prior to any construction or installation work;



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SECTION 2 - REGULATIONS (continued)

2.3 Obligations of the Customer (continued)

(f) complying with all laws and regulations applicable to, and obtaining all consents, approvals, licenses, and permits as may be required with respect to, the location of Company facilities and equipment in any Customer premises or the rights-of-way for which Customer is responsible under section 2.3.1 (d); and granting or obtaining permission for Company agents or employees to enter the premises of the Customer at any time for the purpose of installing, inspecting, maintaining, repairing, or upon termination of service as stated herein, removing the facilities or equipment of the Company.

(g) not creating or allowing to be placed any liens or other encumbrances on the Company's equipment or facilities; and

(h) making Company facilities and equipment available periodically for maintenance purposes at a time agreeable to both the Company and the Customer. No allowance for interruptions in service will be made for the period during which services are interrupted for such purposes.

2.3.2 Claims

With respect to any service or facility provided by the Company, Customer shall indemnify, defend and hold harmless the Company from and against all claims, actions, damages, liabilities, costs and expenses, including reasonable attorneys fees for:

(a) any loss, destruction or damage to property of the Company or any third party, or the death or injury to persons, including, but not limited to employees or invitees of either the Company or the Customer, to the extent caused by or resulting from the negligent or intentional act or omission of Customer, its employees, agents, representatives or invitees; or



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SECTION 2 - REGULATIONS (continued)

2.3 Obligations of the Customer (continued)

(b) any claim, loss, damage, expense or liability for infringement of any copyright, patent, trade secret, or any proprietary or intellectual property right of any third party, arising from any act or omission by the Customer, including, without limitation, use of the Company's services and facilities in a manner not contemplated by the agreement between Customer and Company or this tariff.

2.4 Customer Equipment and Channels

2.4.1 In General

A Customer may transmit or receive information or signals via the facilities of the Company.

2.4.2 Station Equipment

2.4.2.1 The Customer is responsible for providing and maintaining any terminal equipment on the Customer premises. The electric power consumed by such equipment shall be provided by, and maintained at the expense of, the Customer. All such terminal equipment must be registered with the FCC under 47 C.F.R., Part 68 and all wiring must be installed and maintained in compliance with those regulations. The Company will, where practicable, notify the Customer that temporary discontinuance of the use of service may be required; however, where prior notice is not practicable, nothing contained herein shall be deemed to impair the Company's right to discontinue forthwith the use of a service temporarily if such action is reasonable under the circumstances. In case of such temporary discontinuance, the Customer will be promptly notified and afforded the opportunity to correct the condition which gave rise to the temporary discontinuance.



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SECTION 2 - REGULATIONS (continued)

2.4 Customer Equipment and Channels (continued)

2.4.2.2 The Customer is responsible for ensuring that Customer-provided equipment connected to Company equipment and facilities is compatible with such equipment and facilities. The magnitude and character of the voltages and currents impressed on Company-provided equipment and wiring by the connection, operation, or maintenance of such equipment and wiring shall be such as not to cause damage to the Company-provided equipment and wiring or injury to the Company's employees or other persons. Any additional protective equipment required to prevent such damage or injury shall be provided by the Company at the Customer's expense.

2.4.3 Interconnection of Facilities

2.4.3.1 Any special interface equipment necessary to achieve compatibility between the facilities and equipment of the Company used for furnishing Local Exchange Services and the channels, facilities, or equipment of others shall be provided at the Customer's expense.

2.4.3.2 Local Services may be connected to the services or facilities of other communications carriers only when authorized by, and in accordance with, the terms and conditions of the tariffs of the other communications carriers which are applicable to such connections.

2.4.3.3 Facilities furnished under this tariff may be connected to Customer provided terminal equipment in accordance with the provisions of this tariff.



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SECTION 2 - REGULATIONS (continued)

2.4 Customer Equipment and Channels (continued)

2.4.4 Inspections

2.4.4.1 Upon reasonable notification to the Customer, and at a reasonable time, the Company may make such tests and inspections as may be necessary to determine that the Customer is complying with requirements set forth in section 2.4.2.2 for the installations, operation, and maintenance of Customer-provided facilities, equipment, and wiring in the connection of Customer-provided facilities and equipment to Company-owned facilities and equipment.

2.4.4.2 If the protective requirements for Customer-provided equipment are not being complied with, the Company may take such action as it deems necessary to protect its facilities, equipment and personnel. The Company will notify the Customer promptly if there is any need for further corrective action. Within ten days of receiving this notice, the Customer must take this corrective action and notify the Company of the action taken. If the Customer fails to do this, the Company may take whatever additional action is deemed necessary, including the suspension of service, to protect its facilities, equipment, and personnel from harm. The Company will, upon a request from the customer 24 hours in advance, provide the Customer with a statement of technical parameters that the Customer's equipment must meet.



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements

The following provisions shall apply to all service:

2.5.1 Payment for Service

The Customer is responsible for payment of all charges for services furnished by the Company to the Customer or its Joint or Authorized Users. Objections must be received by the Company within 120 days after statement of account is rendered, or the charges shall be deemed correct and binding upon the Customer. A bill will not be deemed correct and binding upon the customer if the Company has records on the basis of which an objection may be considered, or if the customer has in his or her possession such Company records. If an entity other than the Company imposes charges on the Company, in addition to its own internal costs, in connection with a service for which a Company Non-Recurring Charge is specific, those charges may be passed on to the Customer.

2.5.1.1 Taxes

The customer is responsible for the payment of any sales, use, excise, access or other local, state and federal taxes, charges or surcharges (however designated) excluding taxes on the Company's net income, imposed on or based upon the provision, sale or use of Local Services. Any taxes imposed by a local jurisdiction (e.g., county and municipal taxes) will only be recovered from those Customers located in the affected jurisdictions.



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.1.1.1 Other Charges
If an entity other than the Company (e.g. another carrier or a supplier) imposes charges on the Company, in addition to its own internal costs, in connection with a service for which the Company's non-recurring charge is specified, those charges will be passed on to the Customer. It shall be the responsibility of the Customer to pay any such taxes that subsequently became applicable retroactively.

2.5.2 Billing and Collection of Charges

Bills will be rendered monthly to Customer.

2.5.2.1 All service, installation, monthly Recurring, and Non-Recurring Charges are due and payable upon receipt.

2.5.2.2 The Company shall present invoices for Recurring Charges monthly to the Customer, in advance of the month in such service is provided.

2.5.2.3 For new customers or existing customers whose service is disconnected, the charge for the fraction of the month in which service was furnished will be calculated on a pro rated basis. For this purpose every month is considered to have 30 days.

2.5.2.4 A check return charge will be assessed for checks with insufficient funds or non-existing accounts.



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.3 Disputed Bills

The Customer shall notify the Company of any disputed items on a bill in accordance with 26 S.C. Code Ann. Regs. 103-623 (Supp. 1999). If the Customer and the Company are unable to resolve the dispute to their mutual satisfaction, the Customer may file a complaint with the Public Service Commission in accordance with the Commission's rules of procedure.

2.5.3.1 The date of the dispute shall be the date the Company receives sufficient documentation to enable it to investigate the dispute.

The date of the resolution is the date the Company completes its investigation and notifies the Customer of the disposition of the dispute.

2.5.4 Advance Payments

Reserved for future use.



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.5 Deposits

2.5.5.1 Applicants for service or any existing Customer whose financial condition is not acceptable to the Company, or is not a matter of general knowledge, may be required at any time to provide the Company a security deposit. The deposit requested will be in cash or the equivalent of cash, and will be held as a guarantee for the payment of charges. A deposit does not relieve the Customer of the responsibility for the prompt payment of bills on presentation. The deposit will not exceed an amount equal to:

(a) two month's charges for service or facility which has a minimum payment period of one month; or

(b) in accordance with 26 S.C. Code Ann. Regs. 103-621.2 (Supp. 1999).



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.5.2 When a service or facility is discontinued, the amount of a deposit, if any, will be applied to the Customer's account and any credit balance remaining will be refunded. Before the service or facility is discontinued, the Company may, at its option, return the deposit or credit to the Customer's account.

2.5.5.3 Deposits held for residential and business customers will accrue interest in accordance with 26 S.C. Code Ann. Regs. 103-621.3 (Supp. 1999).

2.5.5.4 Deposits from New or Existing Residential Customers Receiving Public Assistance.

The Company shall not require any person it knows to be a recipient of public assistance, supplementary security income, or additional state public assistance payments to post a deposit.



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.6 Discontinuance of Service

2.5.6.1 Upon non payment of any amounts owing to the Company, the Company may, by giving five days' prior written notice served personally upon the Customer; eight days written notice in postpaid wrapper; or five days after the Customer signs or refuses a registered letter containing written notice, suspend service without incurring any liability.

2.5.6.2 Upon violation of any of the other material terms or conditions for furnishing service, the Company may, by giving 30 days prior notice in writing to the Customer, discontinue or suspend service without incurring any liability, if such violation continues during the 30 day period.

2.5.6.3 Upon condemnation of any material portion of the facilities used by the Company to provide service to a Customer or if a casualty renders all or any material portion of such facilities inoperable beyond feasible repair, the Company, by notice to the Customer, may discontinue or suspend service without incurring any liability.

2.5.6.4 Upon the Customer's insolvency, assignment for the benefit of creditors, filing for bankruptcy or reorganization, failing to discharge and involuntary petition within the time permitted by law, or abandonment of service, the Company may, with prior notice to the Customer, immediately discontinue or suspend service without incurring any liability.

2.5.6.5 Upon any governmental prohibition or required alteration of the services to be provided or any violation of any applicable law or regulation, the Company may immediately discontinue service without incurring any liability.



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.6 Discontinuance of Service (continued)

2.5.6.6 The Company may discontinue the furnishing of any and/or all service(s) to a Customer, without incurring any liability.

2.5.6.6.1 Immediately and without notice if the Company deems that such action is necessary to prevent or to protect against fraud or to otherwise protect its personnel, agents, facilities or services. The Company may discontinue service pursuant to this sub-section 2.5.6.6.1 (a-f) if;

(a) The Customer refuses to furnish information to the Company regarding the Customer's credit-worthiness, its past or current use of common carrier communications services or its planned use of service(s); or

(b) The Customer provides false information to the Company regarding the Customer's identity, address, credit-worthiness, past or current use of common carrier communications services, or its planned use of the Company's service(s); or

(c) The Customer has been given written notices as described in Section 2.5.6.1 by the Company of any past due amount (which remains unpaid in whole or part) for any of the Company's other common carrier communications services to which the Customer either subscribes or has subscribed to use; or



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.6 Discontinuance of Service (continued)

2.5.6.6 (continued)

2.5.6.6.1 (continued)

(d) The Customer uses or attempts to use service with the intent to avoid the payment, either in whole or in part, of the tariffed charges for the service by:

(d.1) Using or attempting to use service by rearranging, tampering with, or making connection to the Company's service not authorized by this tariff; or

(d.2) Using tricks, schemes, false or invalid numbers, false credit devices, electronic devices; or

(d.3) Any other fraudulent means or devices; or

(e) Use of Service in such a manner as to interfere with the services of other users; or

(f) Use of service for unlawful purposes.

2.5.6.6.2 Immediately upon written notice to the Customer of any sum thirty (30) days past due;

2.5.6.6.3 Upon ten (10) days written notice to the Customer, after failure of the Customer to comply with a request made by the Company for security for the payment of service in accordance with Section 2.5.5; or



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.6 Discontinuance of Service (continued)

2.5.6.6.4 Ten (10) days after sending the Customer written notice of noncompliance with any provision of this tariff if the noncompliance is not corrected within the ten (10) day period; or

2.5.6.6.5 Upon five (5) days written notice, excluding Sundays and holidays, for non-payment of a bill for service.

2.5.6.7 The suspension of discontinuance of service(s) by the Company pursuant to this Section does not relieve the Customer of any obligation to pay the Company for charges due and owing for service(s) furnished during the time of or up to suspension or discontinuance.

2.5.6.8 Upon the Company's discontinuance of service to the Customer under section 2.5.6.1 or 2.5.6.2, all applicable charges, including termination charges, shall become due. This is in addition to all other remedies that may be available to the Company at law or in equity or under any other provision of this tariff.



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.6 Discontinuance of Service (continued)

2.5.6.9 Termination of Residential Service shall not be made until:

(a) At least 10 days after written notification has been served personally on the Customer, or
(b) At least 13 days after written notification in a postpaid wrapper has been mailed to the billing address of the Customer, or
(c) At least 10 days after the Customer has either signed for or refused a registered letter containing written notification mailed to the billing address of the customer, or
(d) A Deferred Payment Agreement has been offered to a Customer
(e) Termination notices may not be issued until at least 25 days after the date of the bill unless exceptional circumstances exist and then only in accordance with Commission approved procedures. Bills must be mailed to Customers no later than six business days after the date of the bill. The 25-day period shall be extended on day for each day beyond the sixth business day when bills are mailed late.
(f) Termination shall not be made until at least 20 days after written notification has been issued.
(g) Termination may occur only between the hours of 8AM and 4PM Monday through Thursday, provided that such day or the following day is not a public holiday or a day on which the Company's offices are closed. In addition, service may not be disconnected on December 23 through 26 and December 30 through January 2. At least one attempt shall be made during non-working hours to contact the Customer by telephone before the date of termination.



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SECTION 2 - REGULATIONS (continued)

2.5 Payment Arrangements (continued)

2.5.6 Discontinuance of Service (continued)

2.5.6.10 The following will apply for the termination of residential service:

(a) For medical emergencies, an additional 30 days will be allowed for Customers before termination, provided a medical certificate is supplied. The medical emergency status may be extended beyond 30 days, upon submission of required documentation. During the pendency of the emergency, Customers will be able to defer payment of monthly charges in an amount set by the Commission until the emergency ceases or it is determined that Customers have the ability to pay the charges.

(b) Where a Customer is identified to the Company as being blind, disabled or 62 years or age or older and all other occupants of the household are under 18 years of age, or 62 years of age or older, blind or disabled, an additional 30 days will be allowed before termination may occur. The Company shall make a diligent effort to contact by phone or in person an adult resident at the location for purposes of devising a payment plan eight days before the date of termination.

2.5.7 Interest on Customer Overpayments

A Customer who makes a payment to the Company in excess of the Correct charge for telephone service, which overpayment was caused by erroneous billing by the Company, shall be paid interest on the amount of the overpayment. The rate of interest on such amount shall be prescribed by the Commission in accordance with 26 S.C. Code Ann. Regs. 103-623.1 (Supp. 1999).



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SECTION 2 - REGULATIONS (continued)

2.6 Allowances for Interruptions in Service

2.6.1 Credit for Interruptions: When the use of service or facilities furnished by the Company is interrupted due to any cause other than the negligence or willful act of the Customer, or the operation or failure of the facilities or equipment provided by the Customer, a pro rata adjustment of the monthly Recurring Charges subject to interruption will be allowed for the service and facilities rendered useless and inoperative by reason of the interruption, whenever said interruption continues for a period of 24 hours or more from the time the interruption is reported to or known to exist by the Company, except as otherwise specified in the Company's tariffs. If the Customer reports a service, facility or circuit to be inoperative but declines to release it for testing and repair, it is considered to be impaired, but not interrupted.

For calculating credit allowances, every month is considered to have 30 days. A credit allowance is applied on pro-rata basis against the rates specified hereunder for Local Line or Local Trunk Service and is dependent upon the length of the interruption. Only those facilities on the interrupted portion of the circuit will receive a credit. Credit allowances for service outages that exceed 24 hours in duration will be rounded up at the next whole 24 hours.

2.6.2 Limitations on Allowances

No credit allowance will be made for:

(a) interruptions due to the negligence of, or noncompliance with the provisions of this tariff by, the Customer, Authorized User, Joint-User, or other common carrier providing service connected to the service of Company;

(b) interruptions due to the negligence of any person other than the Company including, but not limited to, the Customer or other common carriers connected to the Company's facilities;



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SECTION 2 - REGULATIONS (continued)

2.6 Allowances for Interruptions in Service (continued)

2.6.2 Limitations on Allowances (continued)

(c) interruptions due to the failure or malfunction of non-Company equipment;

(d) interruptions of service during any period in which the Company is not given full and free access to its facilities and equipment for the purpose of investigating and correcting interruptions;

(e) interruptions of service during a period in which the Customer continues to use the service on an impaired basis;

(f) interruptions of service during any period when the Customer has released service to the Company for maintenance purposes or for implementation of a Customer order for a change in service arrangements;

(g) interruption of service due to circumstances or causes beyond the control of the Company.

2.6.3 User of Alternative Service Provided by the Company: Should the Customer elect to use an alternative service provided by the Company during the period that a service is interrupted, the Customer must pay the tariffed rates and charges for the alternative services used.



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SECTION 2 - REGULATIONS (continued)

2.7 Cancellation of Service

2.7.1 Cancellation of Applications for Service

The following provisions shall apply to all service offerings:

2.7.1.1 Unless the Company breeches its obligations, applications for service are non-cancelable after 48 hours, unless the Company otherwise agrees. Where the Company permits Customer to cancel an application for service prior to the start of service or prior to any special construction, no charges will be imposed except for those specified below.

2.7.1.2 Where prior to cancellation by the Customer, the Company incurs any expenses in installing the service or in preparing to install the service that it otherwise would not have incurred, a charge equal to the costs the company incurred, less net salvage, shall apply, but in no case shall this charge exceed the sum of the charge for the minimum period of service ordered, including installation charges, and all charges others levy against the Company that would have been chargeable to the Customer had service begun.

2.7.1.3 The special charges described in 2.7.1.1 and 2.7.1.2 will be calculated and applied on a case-by-case basis.

2.7.2 Cancellation of Service by the Customer

If a Customer cancels a Service Order or terminates services before the completion of the term for any reason whatsoever other than a service interruption (as defined in 2.6.1 above), Customer agrees to pay to Company the following sums which shall become due and owing as of the effective date of the cancellation or termination and payable within the period set forth in 2.5.5, all costs, fees and expenses incurred in connection with:



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SECTION 2 - REGULATIONS (continued)

2.7.2 Cancellation of Service by the Customer (cont.)

1) all Non-Recurring Charges reasonably expended by the Company to establish service to Customer, plus

2) any disconnection, early cancellation or termination charges reasonably incurred and paid to third parties by Company on behalf of Customer, plus

3) all Recurring Charges specified in the applicable Service Order tariff for the balance of the then current term.

2.8 Transfers and Assignments

Neither the Company nor the Customer may assign or transfer its rights or duties in connection with the services and facilities provided by the Company without the written consent of the other party, except that the Company may assign its rights and duties (a) to any subsidiary, parent company or affiliate of the Company (b) pursuant to any sale or transfer of substantially all assets of the Company; (c) pursuant to any financing, merger or reorganization of the Company.

2.9 Notices and Communications

2.9.1 The Customer shall designate on the Service Order an address to which the Company shall mail or deliver all notices and other communications, except that Customer may also designate a separate address to which the Company's bills for service shall be mailed.

2.9.2 The Company shall designate on the Service Order an address to which the Customer shall mail or deliver all notices and other communications, except that Company may designate a separate address on each bill for service to which the Customer shall mail payment on that bill.



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SECTION 2 - REGULATIONS (continued)

2.9.3 All notices or other communications required to be given pursuant to this tariff will be in writing. Notices and other communications of either party, and all bills mailed by the Company, shall be presumed to have been delivered to the other party on the third business day following placement of the notice, communications, or bill with the U.S. Mail or a private delivery service prepaid and properly addressed, or when actually received or refused by the Addressee, whichever occurs first.

2.9.4 The Company or the Customer shall advise the other party of any changes to the addresses designated for notices, other communications or billing, by following the procedures for giving notice set forth herein.



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# SECTION 3 - SERVICE DESCRIPTIONS

## 3.1 Local Exchange Service

The Company's Local Telephone Service provides a Customer with the ability to connect to the Company's switching network which enables the Customer to:

- place or receive calls to any calling Station in the Local calling area, as defined herein;
- access 911 Emergency Service;
- access the interexchange carrier selected by the Customer for interLATA, intraLATA, interstate or international calling;
- access Operator Services
- access Directory Assistance for the local calling area;
- place or receive calls to 800 telephone numbers;
- access Telecommunication Relay Service

The Company's service cannot be used to originate calls to other telephone companies' caller-paid information services (e.g., 900, 976). Calls to those numbers and other numbers used for caller-paid information services will be blocked by the Company's switch.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.1 Local Exchange Service (continued)

3.1.1 Exchange Service Areas

Local exchange services are provided, subject to availability of facilities and equipment, in areas currently served by the following Incumbent LECs:

1) BellSouth Telecommunications
2) Verizon Communications

3.1.1.1 Rate Groups

Charges for local services provided by the Company may be based, in part, on the Rate Group associated with the Customers End Office. The Rate Group is determined by the total access lines and PBX trunks in the local calling area which can be reached from each End Office.

| Rate Group | Exchange Access Lines and PBX Trunks In Local Calling Area - Upper Limit |
|---|---|
| 1 | up to 7,000 |
| 2 | 7,001 up to 15,000 |
| 3 | 15,001 up to 28,500 |
| 4 | 28,501 up to 50,000 |
| 5 | 50,001 up to 78,000 |
| 6 | 78,001 up to 125,000 |
| 7 | 125,001 + |



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.1 Local Exchange Service (continued)

3.1.2 Local Line: Local Line provides the Customer with a single, voice-grade communications channel. Each Local Line will include a telephone number.

3.1.2.1 Standard Features: Each Local Line Customer is provided with the following standard features:

Touch Tone
Direct Inward Dialing
Direct Outward Dialing
Hunt Groups

3.1.2.2 Optional Features: A local Business Customer may order the following optional features. At the rates specified in Section 7. Residential rates are set forth in Section 6 following.

Call Forwarding
Call Pick-up
Call Transfer
Call Waiting
Code Restrictions
Three-Way calling (conference calling)
Six-Way calling (conference calling)
Caller ID
Project Account Codes, non-verified
Project Account Codes, verified
Voicemail

3.1.2.3 Local Line Rates and Charges: A Local Line Customer will be charged applicable Non-Recurring Charges, monthly Recurring Charges and usage charges as specified in Section 7. Customers will be notified of all applicable rates, terms and conditions for local exchange services.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.1 Local Exchange Service (continued)

3.1.2 Local Line (continued)

3.1.2.3 Local Line Rates and Charges (continued)

A. Non-Recurring Charges

| | Bellsouth Areas | | Verizon Areas | |
|---|---|---|---|---|
| | Residential | Business | Residential | Business |
| Line Connection Charge | | | | |
| First line | 40.00 | 64.00 | 44.00 | 54.00 |
| Each add'l line | 18.00 | 26.00 | 44.00 | 54.00 |
| Service Order Charge | 18.00 | 26.00 | 24.00 | 28.00 |
| Line/Trunk Change Charge | | | | |
| First Line | 22.50 | 25.00 | 24.00 | 28.00 |
| Each add'l line | 12.00 | 9.00 | 24.00 | 28.00 |
| Record Order Charge | 5.25 | 10.00 | 5.25 | 10.00 |
| PIC-2 Change (per line) | 10.00 | 10.00 | 10.00 | 10.00 |
| Line Restoral Charge | | | | |
| First Line | 40.00 | 64.00 | 44.00 | 54.00 |
| Each add'l line | 18.00 | 26.00 | 44.00 | 54.00 |
| Restoration Charge[1] | 85.00 | 85.00 | 25.00 | 25.00 |
| Premises Work Charge | | | | |
| First 15 minutes | 22.00 | 23.00 | 15.0 | 15.00 |
| Each add'l 15 mins | 11.00 | 11.00 | 10.00 | 10.00 |

[1] Applies for line restoral after Customer-initiated suspension



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.1 Local Exchange Service (continued)

3.1.3 Usage Rates: All Local Exchange Service Customers must order service on a per minute usage basis. Following are three (3) calling options. These rates will apply to all outgoing direct-dialed calls placed to Stations within the caller's local exchange area, as defined herein.

Option 1
Option 1 rates are postalized rates (single rate) regardless of the mileage associated with an intraLATA call. There is a peak and off-peak rate (see following for definition of peak & off-peak). Option 1 Toll Rates mirror the Customer's Local Service usage rates. Therefore, the customer is billed one rate for both local and interLATA calls.

Option 2
Option 2 establishes postalized peak and non-peak rate for all non-local calls.

Option 3
Option 3 establishes a peak/non-peak rate based upon the Customer's dialing pattern. For example, all calls made within a LATA dialing seven (7) digits will have a distinct rate from those calls made within a LATA dialing eleven (11) digits.

3.1.4.1 Per Minute Usage Rate: Rates are set forth in Section 7.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.1 Local Exchange Service (continued)

3.1.4.2 Timing of Local Exchange Calls

Unless otherwise indicated, all calls are timed in six-second increments and all calls that are fractions of a minute are rounded up to the next six-second increment.

For station-to-station calls, call timing begins when a connection is established between the calling telephone and the called telephone station.

For person-to-person calls, call timing begins when connection is established between the calling person and the particular person, station or mobile unit specified or an agreed alternate.

Call timing ends when the calling station "hangs up", thereby releasing the network connection. If the called station "hangs up" but the calling station does not, chargeable time ends when the network connection is released either by automatic timing equipment in the telephone network or by the Company operator.

3.1.4.2.1 Time Periods Defined

Peak: 8:00 a.m. to, but not including 5:00 p.m. - Monday through Friday

Off-Peak: 5:00 p.m. to, but not including 8:00 a.m. - Monday through Friday, all day Saturday and Sunday, and all Holidays.

Holidays include Christmas, New Year's Day, Thanksgiving, Independence Day, and Labor Day.

All times refer to local time.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.2 Directory Assistance

A Customer may obtain Directory Assistance in determining telephone numbers within its local calling area by calling the Directory Assistance operator.

3.2.1 Each call to Directory Assistance will be charged as follows:

| | Per Call |
|---|---|
| Bellsouth Service Areas | $1.25 |
| Verizon Service Areas | $0.40 (local) |
| | $0.95 (national) |

The Customer may request a maximum of two telephone numbers per call to Directory Assistance service.

3.2.2 A credit will be given for calls to Directory Assistance as follows:

- The Customer experiences poor transmission or is cut-off curing the call;

or

- The Customer is given an incorrect telephone number.

To obtain such a credit, the Customer must notify its Customer Service representative within 24 hours of occurrence.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.3 Operator Assistance

A Customer may obtain the assistance of a local operator to complete local exchange telephone calls in the following manner. Rates applicable to the following services are:

Third Number Billing: Provides the Customer with the capability to charge a local call to a third number which is different from the called or calling party. The party answering at the third number has the option to refuse acceptance of the charges in advance or when queried by the operator.

Collect Calls: Provides the Customer with the capability to charge a call to the called party. On the operator announcement of a collect call, the called party has the option to refuse acceptance of charges in advance or when queried by the operator.

Calling Cards: Provides the Customer with the capability to place a call using a calling card of an Interexchange Carrier with or without the assistance of an operator.

Person to Person: Calls completed with the assistance of any operator to a particular Station and person specified by the Caller. The call may be billed to the called party.

Station to Station: Calls completed with assistance of an operator to a particular Station. The call may be billed to the called party.

General Assistance: The Customer has the option to request general information from the operator, such as dialing instructions, country or city codes, area code information and Customer Service 800 Telephone numbers, but does not request the operator to complete a call.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.3 Operator Assistance (continued)

3.3.1 Busy Line Verification and Interrupt Service: Service is currently not available. Busy Line Verification and Interrupt Service, which is furnished where and to the extent that facilities permit, provides the customer with the following options:

3.3.1.1 Busy Line Verification: Upon request of the calling party, the Company will determine if the line is clear or in use and report to the calling party.

3.3.1.2 Busy Line Verification with Interrupt: The operator will interrupt the call on the called line only if the calling party indicates an emergency and requests interruption.

3.3.1.3 Rates: Rates for Busy Line Verification and Interrupt Service will apply under the following circumstances:

3.3.1.3.1 The operator verifies that the line is busy with a call in progress.

3.3.1.3.2 The operator verifies that the line is available for incoming calls.

3.3.1.3.3 The operator verifies that the called number is busy with a call in progress and the Customer requests interruption. The operator will then interrupt the call, advising the called party the name of the calling party. One charge will apply for both verification and interruption, charges are set forth in Section 7.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.4 Directory Listings

The Company shall provide for a single directory listing, termed the primary listing, in the telephone directory published by the dominant local exchange service provided in the Customer's exchange area of the Station number which is designated as the Customer's main billing number. Directory listings of additional Company Station numbers, other than the Customer's main billing number, associated with a Customer's service will be provided for a monthly recurring charge per listing.

3.4.1 The Company reserves the right to limit the length of any listing in the directory by the use of abbreviations when, in its judgment, the clearness of the listing or the identification of the Customer is not impaired thereby. Where more than one line is required to properly list the Customer, no additional charge is made.

3.4.2 The Company may refuse a listing which is known to constitute a legally authorized or adopted name, obscenities in the name, or any listing which, in the opinion of the Company, is likely to mislead or deceive calling persons as to the identity of the listed party, or is a contrived name used for advertising purposes or to secure a preferential position in the directory or is more elaborate than is reasonably necessary to identify the listed party. The Company, upon notification to the Customer, will withdraw any listing which is found to be in violation of its rules with respect thereto.

3.4.3 Each listing must be designated Government or Business to be placed in the appropriate section of the directory. In order to aid the user of the directory, and to avoid misleading or deceiving the calling party as to the identity of the listed party, only business listings may be placed in the Business Section and only residential listings in the Residential Section. The Company, upon notification to the Customer, will withdraw any listing which is found to be in violation of its rules and respect thereto.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.4 Directory Listings (continued)

3.4.4 In order for listings to appear in an upcoming directory, the Customer must furnish the listing to the Company in time to meet the directory publishing schedule.

3.4.5 Directory listings are provided in connection with each Customer service as specified herein.

3.4.5.1 Primary Listing: A primary listing contains the name of the Customer, or the name under which a business is regularly conducted, as well as the address and telephone number of the Customer. This listing is provided at no additional charge.

3.4.5.2 Additional Listings: In connection with business service, additional listings are available only in the names of the Authorized Users of the Customer's service, as defined herein. Rates for additional listings are specified in Section 3.4.5.8.

3.4.5.3 Non-published Listings: Listings that are not printed in directories or available from Directory Assistance.

A Non-published Telephone Service will be furnished, at the Customer's request, providing for the omission or deletion of the Customer's telephone listing from the telephone directory and, in addition, the Customer's telephone listing will be omitted or deleted from the directory assistance records, subject to the provisions set forth in Section 2.1.4. Rates for Non-published listings are specified in Section 7.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.4 Directory Listings (continued)

3.4.5.4 Non-listed Numbers: A Non-listed number will be furnished at the Customer's request, providing for the omission or deletion of the Customer's listing from the telephone directory. Such listings will be carried in the Company's directory assistance and other records and will be given to any calling party. Charges for Non-listed numbers are specified in Section 7.

3.4.5.5 Foreign Listings: Where available, a listing in a telephone directory which is not in the Customer's immediate calling area. The Customer will be charged the rates specified in the tariff published by the specific local exchange carrier providing the Foreign Listing.

3.4.5.6 Alternate Call Listings: Where available, a listing which references a telephone number which is not the primary listing for the Customer. The Customer must provide written verification that the alternate telephone number is authorized to accept calls.

3.4.5.7 Reference Listings: A listing including additional telephone numbers of the same or another customer to be called in the event there is no answer from the Customer's telephone. Charges for reference listings are specified in Section 7.

3.4.5.8 Recurring Charges: Monthly Recurring Charges associated with Directory Listings are set forth in rate schedule attachments.



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SECTION 3 - SERVICE DESCRIPTIONS (continued)

3.5 Emergency Services: Both Basic and Enhanced 911 (E911) allow Customers to reach appropriate emergency services including police, fire and medical services. Subject to availability, Enhanced 911 has the ability to selectively route an emergency call to the primary E911 provider so that it reaches the correct emergency service located closest to the caller. In addition, the Customer's address and telephone information will be provided to the primary E911 provider for display at the Public Service Answering Point (PSAP).

3.6 Presubscriptions-2 (PIC-2): PIC-2 allows Customers to presubscribe to their carrier of choice for intraLATA calls, without dialing the Access Code. The rates specified in Section 7 will apply each time the Customer requests a change to their intraLATA PIC, subsequent to the initial designation.

3.7 Vanity Telephone Numbers: Service currently not available. At the request of the Customer, the Company may be assigned a telephone number with the last four digits selected by the Customer. The assignment is subject to availability of a particular number and subject to the terms and conditions set forth in Section 2.1.3. Rates are set forth in Section 7.

3.8 Relay South Carolina – 711: This free service connects people using a TTY (text telephone) who are deaf, hard-of-hearing or speech disabled with a standard telephone. The relay operator (OPR) "relays" the conversation between the two. A Customer will be able to access the state provider(s) to complete such calls. Local relay calls placed from any telephone or a payphone are free. The user will be responsible for the long distance charges. A Customer will be able to access the state provider(s) to complete such calls.



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## SECTION 4 - PROMOTIONAL OFFERINGS

4.1 Promotional Offerings: The Company may make promotional offerings to its service which may include waiving or reducing the applicable charges for the promoted service. The promotional offerings may be limited as to the duration, the date and times of the offering and the locations where the offerings are made. These promotional offerings will be filed with the Commission at a minimum of 14 days prior to their effective date.



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## SECTION 5 - INDIVIDUAL CASE BASE (ICB) ARRANGEMENTS

5.1 Individual Case Base (ICB) Arrangements: Competitive pricing arrangements at negotiated rates may be furnished, upon prior Commission approval, on an individual case basis (ICB) in response to request by customers to Company, for proposals or for competitive bids. Service offered under this tariff provision will be provided to the Customer pursuant to contract. Unless otherwise specified, the regulations for such arrangements are in addition to the applicable regulations and prices in other sections of this tariff. Specialized rates or charges will be made available to similarly situated Customers on a non-discriminatory basis.



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## SECTION 6 - LOCAL SERVICE OFFERING

### 6.1 Life Line - Residence

Applies reduced monthly recurring rates (as set forth in 7, following) for qualifying the Company's Access Local Line - Residence service Customers. The basic Life Line monthly rate includes Local Line - Residential measured service. The Interstate Line Charge will be waived for Life Line customers. For connection of new service, Non-Recurring service charges will apply. To qualify for Life Line services a subscriber must be certified as income eligible for benefits under at least one of the following Entitlement Programs administered by the State Department of Social Services:

- Home Relief
- Supplemental Security Income (SSI)

Applicants must provide proof to the Company that they are certified as income eligible to receive one or more of the above benefits. After initial contact, the customer is sent an application form to be completed by the Customer or his authorized representative, as designated by the State Department of Social Services and identified as so authorized on the Customer's card for any of the above benefits.



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## SECTION 6 - LOCAL SERVICE OFFERING

6.1 Life Line - Residence (continued)

In addition, applicants are eligible for discounted Life Line rates when approved to receive either a Veterans Disability Pension or Veterans Surviving Spouse Pension. Applicants must provide proof to the Company that they are receiving one of these pensions.

The Life Line services are effective upon receipt of a completed and signed form, including a pre-printed reply form as specified below or an application form certified from an entity authorized by the Company. If the form is not returned, no further action is taken by the Company to establish eligibility. The Life Line discount is credited as of the service connection date.

An individual's eligibility may be documented by information obtained by the Company as a result of enrollment programs, including but not limited to, confidential computerized matching programs, conducted by the Company in conjunction with the State Department of Social Services.

The Company will upon learning from State Department of Social Services that a Customer is eligible for Life Line but is not currently enrolled in the program, and after providing a period of 30 days from the date the customer was notified of eligibility for the program for the Customer to decline enrollment, convert the Customer's service to Life Line reduced rate service without a signed application. The Life Line services are effective as of the date 30 days from the date of the notice.



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SECTION 6 - RESIDENTIAL SERVICE OFFERING

6.1 Life Line Service (continued)

Applicants who are not identified as current customers, according to a confidential computer matching program conducted with State Department of Social Services may enroll by submitting a pre-printed reply form, approved by the Company and State Department of Social Services, that shows current eligibility information. For new Customers, the Life Line discount is credited as of the service connection date.

The Company, in coordination with State Department of Social Services, will review eligibility status monthly. If, after verification, a Customer is identified as being ineligible, after four consecutive monthly matches when verification is by computerized matching programs, proof of eligibility within thirty days. Upon failure to provide proof to the Company within the specified time period, the Customer's service will be switched to comparable service at full rate. Basic Life Line service will be switched to measured rate service. There will be no charge for a change in service.

Eligibility Information learned from State Department of Social Services in a computerized matching program is confidential, and will not be used for any other purpose than the administration of Life Line Service.



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# SECTION 7 – LOCAL EXCHANGE SERVICES

## 7.1 General

Services provided in this tariff section arc available on an Resale Service basis. Local Resale Services are provided through the use of resold switching arid transport facilities obtained from Other Telephone Companies.

The rates, terms and conditions set forth in the section are applicable where the Company provides specified local exchange services to Customers through resale of BellSouth local exchange services. The rates, terms and conditions set forth in this Section 7 are not applicable to the Company's provision of service within the service area of any other incumbent local exchange carrier or where the Company provides service, in whole or in part, over its own facilities (OnNet). The rates, terms and conditions set forth in this Section 7 are available on a retail basis only and will not be provided for resale to any other carrier.

All rates set forth in this Section 7 are subject to change and may changed by the Company pursuant to notice requirements established by the South Carolina Public Service Commission. The rates, terms and conditions set forth in this Section 7 are applicable as of the effective date hereof and will not apply to any Customer whose services may have been provisioned through resale of BellSouth's local exchange services, in whole or in part, prior to the effective date hereof.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.2 Standard Residence Local Exchange

Standard Residence Local Exchange Service provides the Customer with a single, analog, voice-grade telephonic communications channel which can be used to place or receive one call at a time. Standard Residence Local Exchange Service lines are provided for the connection of Customer-provided wiring, telephones, facsimile machines or other station equipment. An optional per line Hunting feature is available for multi-line Customers which routes a call to the next idle line in a prearranged group when the called line is busy.

Local exchange service tines and trunks are provided on a single party (individual) basis only. No multi-party lines are provided. Service is available on a flat rate, measured rate or message rate basis depending on the service plan selected by the Customer. Not all service plans will be available in all areas.

Recurring charges for Standard Residence Local Exchange Service are billed monthly in advance. Usage charges, if applicable are billed in arrears. Usage charges may apply for calls placed from the Customer's line. No usage charges will apply to calls received by the Customer. Nonrecurring charges for installation or rearrangement of service are billed on the next month's bill immediately following work performed by the Company.



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SECTION 7 – LOCAL EXCHANGE SERVICE (CONT'D)

7.2 Standard Residence Local Exchange Service (Cont'd.)

7.2.1 Monthly Recurring Charges

The following charges apply to Standard Residence Local Exchange Services lines per month. Rates and charges include Touchtone Service for each line. The rates arid charges below apply to service provided on a month-to-month basis.

A. Bellsouth Service Areas

| | Service Types | |
|---|---|---|
| | Flat Rate | Residential Area Package[1] |
| Rate Class 1 | 12.70 | 7.00 |
| Rate Class 2 | 13.15 | 7.00 |
| Rate Class 3 | 13.60 | 7.00 |
| Rate Class 4 | 14.05 | 7.00 |
| Rate Class 5 | 14.50 | 7.00 |
| Rate Class 6 | 14.95 | 7.00 |
| Rate Class 7 | 15.40 | 7.00 |

[1] Usage rates apply as directed in Section 7.2.3



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## SECTION 7 – LOCAL EXCHANGE SERVICE (CONT'D)

### 7.2 Standard Residence Local Exchange Service (Cont'd.)

#### 7.2.1 Monthly Recurring Charges (Cont'd)

B. Verizon Service Areas

| | Service Types | | |
|---|---|---|---|
| | Flat Rate | Measured Rate | Measured Rate with Block of Time[1] |
| Rate Group 1 | 14.46 | 14.46 | 23.00 |
| Rate Group 2 | 16.40 | 16.40 | 23.00 |

[1] The block of time option will allow 30 hours of calling between applicable MEAS exchanges. Overtime charges shall be applicable for all calls occurring beyond the subscribed block of time.



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.2 Standard Residence Local Exchange Service (Cont'd.)

7.2.2 Other Monthly Recurring Charges

A. <u>Bellsouth Service Areas</u>

Hunting (a/k/a Rotary or Grouping)

The following charges apply to Standard Residence Local exchange lines equipped with Hunting. Rates vary based on Rate Group.

| Rate Group | Hunting Per Line |
|---|---|
| Rate Class 1 | 6.85 |
| Rate Class 2 | 7.08 |
| Rate Class 3 | 7.30 |
| Rate Class 4 | 7.53 |
| Rate Class 5 | 7.75 |
| Rate Class 6 | 7.98 |
| Rate Class 7 | 8.20 |

7.2.3 Usage Sensitive Charges and Allowances

(A) Flat Rate Service

No measured or message charges apply to calls placed or received from Flat Rate service lines. Customers receive unlimited calling within their local calling area.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.2 Standard Residence Local Exchange Service, (Cont'd)

7.2.3 Usage Sensitive Charges and Allowances, (cont'd)

(B)

Residential Area Package – BellSouth Service Areas

The following charges apply for customer dialed and operator handled local calls originated from a line equipped for Residential Area Package service

Local usage in excess of allowances specified for the above packages will be billed in arrears. Usage is billed on a per call basis. Usage is billed in one (1) minute increments with partial minutes counting as one (1) full minute. Peak period rates apply from 8 AM to 5 PM Monday through Friday (excluding holidays), Off-Peak period rates apply to all other times.

| Mileage Band | PEAK | | OFF-PEAK | |
|---|---|---|---|---|
| | Initial Minute | Add'l Minute | Initial Minute | Add'l Minute |
| Basic Service Area | 0.020 | 0.020 | 0.010 | 0.010 |
| Extended Service Area | 0.120 | 0.120 | 0.060 | 0.060 |

Residential Usage Rates – Verizon Service Areas

| Mileage Band | PEAK | | OFF-PEAK | |
|---|---|---|---|---|
| | Initial Minute | Add'l Minute | Initial Minute | Add'l Minute |
| Serving Exchange | 0.0120 | 0.0120 | 0.0120 | 0.0120 |
| All Other Exchanges | 0.0250 | 0.0250 | 0.0250 | 0.0250 |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.2 Standard Residence Local Exchange Service, (Cont'd)

7.2.4 Optional Calling Plans – Verizon Service Areas ONLY (cont'd)

Residential Local Package Extra

A. Description

This service is only available to customers in the Verizon service areas. Residential Local Package Extra provides the customer with unlimited direct-dialed local calling with Extended Area Service, unlimited local directory assistance, plus a choice of up to ten or more of any or all the following calling features:

| | |
|---|---|
| *69 | Distinctive Ring |
| Anonymous Call Block | Do Not Disturb |
| Busy Redial | Priority Call |
| Call Block | Select Call Forwarding |
| Call Forwarding | Speed Dialing 8 |
| Call Waiting/ Cancel Call Waiting | Speed Dialing 30 |
| Caller ID | Three-Way Calling |

Residential Local Package Extra is only available on flat-rated single-line residential service. Residential Local Package Extra is not available with the following:

- any other package or bundled offering on the same line
- Lifeline Assistance
- Local Calling Plans
- any measured or message rate services
- employee concession service
- ISDN Service



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.2 Standard Residence Local Exchange Service, (Cont'd)

7.2.4 Optional Calling Plans – Verizon Service Areas ONLY (cont'd)

Residential Local Package Extra (Cont'd)

B. Rates

Monthly Recurring Charges

| | Rate |
|---|---|
| Individual Line, each | $ 31.95 |

Residential Local Package

A. Description

This service is only available to customers in the Verizon service areas. Residential Local Package provides the customer with unlimited direct-dialed local calling with Extended Area Service, unlimited local directory assistance, plus the following calling features: Caller ID, Call Waiting & Three-Way Calling

Residential Local Package is only available on flat-rated single-line residential service. Residential Local Package is not available with the following:

- any other package or bundled offering on the same line
- Lifeline Assistance
- Local Calling Plans
- any measured or message rate services
- employee concession service
- ISDN Service



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.2 Standard Residence Local Exchange Service, (Cont'd)

7.2.4 Optional Calling Plans – Verizon Service Areas ONLY (cont'd)

Residential Local Package Extra (Cont'd)

B. Rates

Monthly Recurring Charges

| | Rate |
|---|---|
| Individual Line, each | $28.95 |



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

### 7.2 Standard Residence Local Exchange Service, (Cont'd)

#### 7.2.5 Non-Recurring Charges

Non-recurring charges apply to each line installed for the Customer. Non-recurring charges are in addition to applicable service order charges contained in Section 4 of this tariff. All such charges will appear on the next bill following installation of the service.

Non-recurring charges for installation of Residential lines may be found in Section 3.1.2.3.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.3 Standard Business Local Exchange Service

Standard Business Local Exchange Service provides the Customer with a single, analog, voice-grade telephonic communications channel which can be used to place or receive one call at a time. Standard Business Local Exchange Service lines are provided for the connection of Customer-provided wiring, telephones, facsimile machines or other station equipment. An optional per line Hunting feature is available for multi-line Customers which routes a call to the next idle line in a prearranged group when the called line is busy.

Local exchange service lines and trunks are provided on a single party (individual) basis only. No multi-party lines are provided- Service is available on a flat rate, measured rate or message rate basis depending on the service plan selected by the Customer. Not all service plans will be available in all areas,

Recurring charges for Standard Business Local Exchange Service are billed monthly in advance. Usage charges, if applicable are billed in arrears. Usage charges may apply for calls placed from the Customer's line. No usage charges will apply to calls received by the Customer. Nonrecurring charges for installation or rearrangement of service are billed on the next month's bill immediately following work performed by the Company.



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## SECTION 7 – LOCAL EXCHANGE SERVICES CONT'D)

### 7.3 Standard Business Local Exchange Service, (Cont'd)

#### 7.3.1 Monthly Recurring Charges

A. <u>Bellsouth Service Areas</u>

The following charges apply to Standard Business Local Exchange Service lines per month. Rates and charges include Touchtone Service for each line. The rates and charges below apply to service provided on a month-to-month basis.

| | Flat Rate | Business Area Package [1] |
|---|---|---|
| Group 1 | 32.55 | 33.00 |
| Group 2 | 34.25 | 33.00 |
| Group 3 | 35.95 | 33.00 |
| Group 4 | 37.65 | 33.00 |
| Group 5 | 39.35 | 33.00 |
| Group 6 | 41.05 | 33.00 |
| Group 7 | 42.75 | 33.00 |

B. <u>Verizon Service Areas</u>

| | Service Types | | |
|---|---|---|---|
| | Flat Rate | Measured Rate | Measured Rate with Block of Time[2] |
| Rate Group 1 | 30.58 | 30.58 | 39.00 |
| Rate Group 2 | 33.67 | 33.67 | 39.00 |

[1] Optional Calling Plan A calls will be billed based upon the measured rates found in Section 7.3.3.(C) of this tariff.
[2] The block of time option will allow 30 hours of calling between applicable MEAS exchanges. Overtime charges shall be applicable for all calls occurring beyond the subscribed block of time.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.3 Standard Business Local Exchange Service, (Cont'd)

7.3.2 Other Monthly Recurring Charges

A. Bellsouth Service Areas
Hunting (a/k/a Rotary or Grouping)

The following charges apply to Standard Business Local Exchange lines equipped with Hunting. Rates vary based on Rate Group.

| Rate Group | Hunting Per Line |
|---|---|
| Rate Group 1 | 10.65 |
| Rate Group 2 | 10.65 |
| Rate Group 3 | 10.65 |
| Rate Group 4 | 10.65 |
| Rate Group 5 | 10.65 |
| Rate Group 6 | 10.65 |
| Rate Group 7 | 10.65 |



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SECTION 7 LOCAL EXCHANGE SERVICES (CONT'D)

7.3 Standard Business Local Exchange Service, (Cont'd)

7.3.3. Usage Sensitive Charges and Allowances

(A) Flat Rate Service

No measured or message charges apply to calls placed or received from Flat Rate service lines. Customers receive unlimited calling within their local calling area.



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(B) Business Area Package

The following charges apply for customer dialed and operator handled local calls originated from a line equipped for Business Area Package service

Local usage in excess of allowances specified for the above packages will be billed in arrears. Usage is billed on a per call basis. Usage is billed in one (1) minute increments with partial minutes counting as one (1) full minute. Peak period rates apply from 8 AM to 5 PM Monday through Friday (excluding holidays), Off-Peak period rates apply to all other times.

Bellsouth Service Areas Only

| Mileage Band | PEAK | | OFF-PEAK | |
|---|---|---|---|---|
| | Initial Minute | Add'l Minute | Initial Minute | Add'l Minute |
| Basic Service Area | 0.020 | 0.020 | 0.010 | 0.010 |
| Extended Service Area | 0.120 | 0.120 | 0.060 | 0.060 |

Verizon Service Areas Only

| Mileage Band | PEAK | | OFF-PEAK | |
|---|---|---|---|---|
| | Initial Minute | Add'l Minute | Initial Minute | Add'l Minute |
| Serving Exchange | 0.0120 | 0.0120 | 0.0120 | 0.0120 |
| All Other Exchanges | 0.0250 | 0.0250 | 0.0250 | 0.0250 |



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

### 7.3 Standard Business Local Exchange Service, (Cont'd)

#### 7.3.4 Non-Recurring Charges

Non-recurring charges apply to each line installed for the Customer. Non-recurring charges are in addition to applicable service order charges contained in Section 4 of this tariff. All such charges will appear on the next bill following installation of the service.

Non-recurring charges for installation of Residential lines are:

| | Bellsouth | Verizon |
|---|---|---|
| First Line | $64.00 | 54.00 |
| Each Additional Line[1] | $64.00 | 54.00 |

[1] Additional Line installation charges apply only when 2 or more lines are installed at the same time and at the same Customer Premises.



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

### 7.4 RESERVED FOR FUTURE USE



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

### 7.4 RESERVED FOR FUTURE USE



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.5 Residence and Business PBX Trunk Service

PBX Trunk service provides a Customer with a single, voice-grade telephonic communications channel which can be used to place or receive one call at a time, Trunks are provided for connection of Customer-provided private branch exchanges (PBX) or other station equipment to the public switched telecommunications network.

PBX Trunk's are available to Business and residence Customers as Inward, Outward or Two-Way combination trunks where services and facilities permit. Each PBX Trunk is provided with touch ;one signaling at no additional charge. An optional per trunk Hunting feature is available for Customers which routes a call to the next idle trunk in a prearranged group (see Sections 7.2 and 7.3).

PBX Trunks may also be equipped with Direct Inward Dialing (DID) capability and DID number blocks for additional charges (see Section 7.6).

7.5.1 Verizon Service Areas

| | Flat Rate | | Measured | |
|---|---|---|---|---|
| | Monthly | Non Recurring Charge | Monthly | Non Recurring Charge |
| Rate Group 1, first | 39.99 | 54.00 | 39.99 | 54.00 |
| Each add'l line | 31.21 | n/a | 31.21 | n/a |
| Rate Group 2 | 39.99 | 54.00 | 39.99 | 54.00 |
| Each add'l line | 34.87 | n/a | 34.87 | n/a |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.5 Residence and Business PBX Trunk Service (Cont'd)

7.5.2 Bellsouth Service Areas

| | FLAT RATE | |
|---|---|---|
| | PBX [1] | DID Combination |
| Group 1 | 38.58 | 77.16 |
| Group 2 | 41.13 | 82.26 |
| Group 3 | 43.68 | 87.36 |
| Group 4 | 46.23 | 92.46 |
| Group 5 | 48.78 | 97.56 |
| Group 6 | 51.33 | 102.66 |
| Group 7 | 53.88 | 107.76 |

[1] These rates are applicable for all Inbound, Outbound and Combined PBX Trunks as well as inbound only DID Trunks.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services

7.6.1. Inter-Tel ISDN PRI Service with Unlimited Local Calling

ISDN PRI offers an array of value-added features, such as calling number identification and call-by-call selection that enhance productivity. ISDN PRI is configured with 23 64 Kbps bi-directional B (Bearer) channels and one 64 Kbps D (Data) channel. Unique to ISDN PRI is its ability to designate the D channel to handle all of the signaling and call control requirements and leave the remaining 23 B channels free for any mix of circuit-switched voice and data.

Each of these products is offered under a 12, 24 or 36 month term agreement. Rates include unlimited local calling for sent-paid, directly dialed calls. Rates do not include calling card calls, information type calls to Time and Weather, 555, 700, 900, 976 Services, Directory Assistance or any other type of Operator Handled call.

Inter-Tel ISDN PRI includes the following non-optional Feature Package: Inbound Calling Line ID-Name & Number and Call by Call Selection.

Regional Toll and Long Distance Services must be PIC'd to the Company. These rates are in addition to ISDN PRI and DS1 rates below.

Recurring Charges

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

### 7.6 Advanced Services (Cont'd)

Non-Recurring Charges

| | Non-Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | | | |
| First Line | ICB | ICB | ICB |
| Each Add'l Line | ICB | ICB | ICB |
| Verizon Area | | | |
| First Line | ICB | ICB | ICB |
| Each Add'l Line | ICB | ICB | ICB |
| | | | |
| Expedite Service Charge[1] | Per PRI | | |
| Bellsouth | ICB | | |
| Verizon | ICB | | |
| | | | |
| Order Supplement Charge[2] | First Change | Subsequent Change | |
| Bellsouth | ICB | ICB | |
| Verizon | ICB | ICB | |
| | | | |
| Order Cancellation Charge[Error! Bookmark not defined.] | Per PRI | | |
| Bellsouth | ICB | | |
| Verizon | ICB | | |

[1] Expedite Service Charges apply when customer requests installation of service in less time than normal installation interval of 30 business days.

[2] Order Supplement Charges apply when a change of the Requested Service Date is requested by customer. A change of requested service date must be within 30 days of the previous requested service date. In no event will the Company be obligated to accept more than three (3) changes to a requested service date. The service will be deemed canceled upon the fourth (4) such request and applicable Order Cancellation Charges will apply.



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

### 7.6 Advanced Services (Cont'd)

#### 7.6.2. Inter-Tel Digital DS-1 PBX Service with Unlimited Local Calling

This service provides a trunk side DS1 electrical interface from the customer's digital PBX system to a Inter-Tel digital port on a local Company switch for the origination and termination of calls. Traffic to and from the digital PBX can be received or dialed directly from any PBX station without the need for an attendant.

These digital trunks deliver a high-speed DS1 (T1) connection between your PBX and the Company network. There are up to 24 channels on one facility, each of which can be used to place or receive calls. This multi-channel capability dramatically reduces the need for additional PBX circuit cards.

Each of these products is offered under a 12, 24 or 36 month term agreement. Rates include unlimited local calling for sent-paid, directly dialed calls. Rates do not include calling card calls, information type calls to Time and Weather, 555, 700, 900, 976 Services, Directory Assistance or any other type of Operator Handled call.

Regional Toll and Long Distance Services must be PIC'd to the Company. These rates are in addition to ISDN PRI and DS1 rates below.

Monthly Recurring Charges

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Bell Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

### 7.6 Advanced Services (Cont'd)

Non-Recurring Charges

| | Non-Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | | | |
| First Line | ICB | ICB | ICB |
| Each Add'l Line | ICB | ICB | ICB |
| Verizon Area | | | |
| First Line | ICB | ICB | ICB |
| Each Add'l Line | ICB | ICB | ICB |
| | | | |
| Expedite Service Charge[1] | Per DS1 | | |
| Bellsouth | ICB | | |
| Verizon | ICB | | |
| | | | |
| Order Supplement Charge[2] | First Change | Subsequent Change | |
| Bellsouth | ICB | ICB | |
| Verizon | ICB | ICB | |
| | | | |
| Order Cancellation Charge[Error! Bookmark not defined.] | Per DS1 | | |
| Bellsouth | ICB | | |
| Verizon | ICB | | |

[1] Expedite Service Charges apply when customer requests installation of service in less time than normal installation interval of 30 business days.

[2] Order Supplement Charges apply when a change of the Requested Service Date is requested by customer. A change of requested service date must be within 30 days of the previous requested service date. In no event will the Company be obligated to accept more than three (3) changes to a requested service date. The service will be deemed canceled upon the fourth (4) such request and applicable Order Cancellation Charges will apply.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

7.6.3. Inter-Tel ISDN PRI Service with Unlimited Local Calling and Bundled Toll/LD Service

ISDN PRI offers an array of value-added features, such as calling number identification and call-by-call selection that enhance productivity. ISDN PRI is configured with 23 64 Kbps bi-directional B (Bearer) channels and one 64 Kbps D (Data) channel. Unique to ISDN PRI is its ability to designate the D channel to handle all of the signaling and call control requirements and leave the remaining 23 B channels free for any mix of circuit-switched voice and data.

This product is offered under a 12, 24 or 36 month term agreement. Rates include unlimited local calling for sent-paid, directly dialed calls. Rates do not include calling card calls, information type calls to Time and Weather, 555, 700, 900, 976 Services, Directory Assistance or any other type of Operator Handled call.

The Unlimited Local Calling and Bundled Toll/LD Service Products are offered with six different increments of Toll/LD Minutes of Use: 5,000, 10,000, 15,000, 30,000, 50,000 and 100,000. Installation charges are included in the monthly recurring charges. Regional Toll and Long Distance Services must be PIC'd to the Company.

<u>Inter-Tel ISDN PRI with Unlimited Local and Bundled 5,000 Long Distance MOU</u>
This package includes unlimited local and 5,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 5,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

Inter-Tel ISDN PRI with Unlimited Local and Bundled 10,000 Long Distance MOU
This package includes unlimited local and 10,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 10,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |

Inter-Tel ISDN PRI with Unlimited Local and Bundled 15,000 Long Distance MOU
This package includes unlimited local and 15,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 15,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

Inter-Tel ISDN PRI with Unlimited Local and Bundled 30,000 Long Distance MOU
This package includes unlimited local and 30000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 30,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |

Inter-Tel ISDN PRI with Unlimited Local and Bundled 50,000 Long Distance MOU
This package includes unlimited local and 50,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 50,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

Inter-Tel ISDN PRI with Unlimited Local and Bundled 100,000 Long Distance MOU
This package includes unlimited local and 100,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 100,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |

7.6.4. Inter-Tel Digital DS-1 PBX Service with Unlimited Local Calling and Bundled Toll/LD Service

This service provides a trunk side DS1 electrical interface from the customer's digital PBX system to a Inter-Tel digital port on a local Company switch for the origination and termination of calls. Traffic to and from the digital PBX can be received or dialed directly from any PBX station without the need for an attendant.

These digital trunks deliver a high-speed DS1 (T1) connection between your PBX and the Company network. There are up to 24 channels on one facility, each of which can be used to place or receive calls. This multi-channel capability dramatically reduces the need for additional PBX circuit cards.

Each of these products is offered under a 12, 24 or 36 month term agreement. Rates include unlimited local calling for sent-paid, directly dialed calls. Rates do not include calling card calls, information type calls to Time and Weather, 555, 700, 900, 976 Services, Directory Assistance or any other type of Operator Handled call.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

The Inter-Tel Digital DS-1 PBX Service with Unlimited Local Calling and Bundled Toll/LD Service Products are offered with six different increments of Toll/LD Minutes of Use: 5,000, 10,000, 15,000, 30,000, 50,000 and 100,000. Installation charges are included in the monthly recurring charges. Regional Toll and Long Distance Services must be PIC'd to the Company.

Inter-Tel ISDN DS1 with Unlimited Local and Bundled 5,000 Long Distance MOU
This package includes unlimited local and 5,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 5,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |

Inter-Tel ISDN DS1 with Unlimited Local and Bundled 10,000 Long Distance MOU
This package includes unlimited local and 10,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 10,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

Inter-Tel ISDN DS1 with Unlimited Local and Bundled 15,000 Long Distance MOU
This package includes unlimited local and 15,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 15,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |

Inter-Tel ISDN DS1 with Unlimited Local and Bundled 30,000 Long Distance MOU
This package includes unlimited local and 30000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 30,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

Inter-Tel ISDN DS1 with Unlimited Local and Bundled 50,000 Long Distance MOU
This package includes unlimited local and 50,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 50,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |

Inter-Tel ISDN DS1 with Unlimited Local and Bundled 100,000 Long Distance MOU
This package includes unlimited local and 100,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 100,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

| | Monthly Recurring Charge | | |
|---|---|---|---|
| | 12 Months | 24 Months | 36 Months |
| Bellsouth Area | ICB | ICB | ICB |
| Verizon Area | ICB | ICB | ICB |



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## SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

### 7.6 Advanced Services (Cont'd)

#### 7.6.5. Inter-Tel ISDN BRI Service

Inter-Tel ISDN BRI (Basic Rate Interface) uses standard "twisted pair" cables and is nearly three times faster than a 56K dial up line. Inter-Tel ISDN PRI (Primary Rate Interface) uses a 1.544 Mbps digital transport facility (T1). Both services provide the superior clarity of digital transmission, a high-speed data interface and sufficient bandwidth capacity to fulfill your current and future communication needs.

ISDN BRI consists of two 64 Kbps B (Bearer) channels and one 16 Kbps D (Data) channel. Each B channel has the ability to integrate voice, data, image and video. The B channels may be kept separate or bonded together to deliver 128 Kbps.

Monthly Recurring Charges

| | Monthly Recurring Charge[1] |
|---|---|
| | |
| ISDN Basic Exchange Digital Line, each | $10.00 |
| ISDN Basic Exchange Circuit Switched Voice | |
| First Line | n/a |
| Second Line | 2.00 |
| ISDN Basic Exchange Circuit Switched Data, each | 2.00 |
| ISDN Basic Exchange Alternate Circuit Switched Voice/Data,each | 2.00 |

[1] These ISDN BRI rates are a supplement to individual Message Rate Service.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

7.6.6. Inter-Tel Digital Centrex Service

Inter-Tel Digital Centrex Service delivers superior performance, PBX-like functionality including abbreviated dialing, and is compatible with many telephone sets. Each user has a unique seven-digit direct telephone number and customized features. The service is affordable, power failure safe and provides a scalable platform for future growth and technology.

Monthly Recurring Charges

| Contract Length | Monthly Recurring Charge |
|---|---|
| | |
| 12 months – Assume Dial 9 | 26.61 |
| 12 months | 23.15 |
| 24 months | 21.05 |
| 36 months | 17.59 |
| 60 months | 16.51 |
| 84 months | 15.80 |

**NOTES FOR ALL**: Availability of services must be verified with the Company based on customer address and NPA-NXX. Rates do not included FCC End User Charge, FCC Port Charge, or other surcharges and taxes. Minimum service period is 12 months. If service is cancelled prior to the end of the contract, a termination charge will be calculated as follows: a. The average of the sum of all line charges on three previous Company invoices to the customer (excluding taxes) multiplied by the number of months remaining in the term agreement.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 Advanced Services (Cont'd)

7.6.7. Direct Inward Dialing (DID) Service

DID service is an optional feature which can be purchased in conjunction with Company-provided Basic Trunks or Digital Trunks. DID service transmits the dialed digits for all incoming calls allowing the Customer's PBX to route incoming calls directly to individual stations corresponding to each individual DID number. Charges for DID capability and DID numbers apply in addition to charges specified for Basic Trunks or Digital Trunks.

So the Company may efficiently manage its number resource, the Company, at its sole discretion, reserves the right to limit the quantity of DID numbers a Customer may obtain. Requests for 300 or more DID numbers must be provided to the Company in writing no less than five (5) months prior to activation. In addition, the Company reserves the right to review vacant DID stations or stations not in use to determine their utilization. Should the Company determine, based on its own discretion, that there is inefficient number utilization, the Company may reassign the DID numbers.

The Customer has no property right to the telephone number or any other call number destination associated with DID service furnished by the Company, and no right to the continuance of service through any particular end office. The Company reserves the right to change such numbers, or the end office designation associated with such numbers, or both, assigned to the Customer, whenever the Company deems it necessary to do so in the conduct of its business.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.6 ADVANCED SERVICES (Cont'd)

7.6.7. Direct Inward Dialing (DID) Service (Cont'd)

Verizon Service Areas

| | Monthly Recurring |
|---|---|
| DID Numbers | |
| Block of 20 Numbers | $10.00 |
| Block of 100 Numbers | $50.00 |
| DID Trunk Termination | $15.00 |

Non-Recurring Installation Fee $100.00

Bellsouth Service Areas

| | Monthly Recurring |
|---|---|
| DID Numbers | |
| Block of first 20 numbers | $5.00 |
| Block of add'l 20 numbers | $5.00 |
| DID Trunk Termination | $31.00 |

Automatic Intercept Service, Per Number Referred $16.00



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.7 Access Lines for Customer Provided Pay Telephones ("CPPT Lines")

7.7.1 General

The Company provides access lines for connection of Aggregator provided Pay Telephone equipment to the public switched network.. CPPT Lines provide the Aggregator with a single, analog. voice-grade telephonic communications channel which can be used to place or receive one call at a time. CPPT Lines are provided on a single party (individual) basis only. No multi-party lines are provided.

Recurring charges for CPPT lines are billed monthly in advance. Usage charges, if applicable, are billed in arrears, Usage charges may apply for calls placed from the CPPT Line subscribed to by the Aggregator. No usage charges will apply to calls received by the Customer. Non-recurring charges for installation or rearrangement of service are billed on the next month's bill immediately following work performed by the Company.

7.7.2 Regulations

(A) CPPT Lines will be provided only to Aggregators certificated by the South Carolina Public Service Commission. Proof of certification is required prior to installation of service, Service will be disconnected should the Company determine that the Aggregator is no longer certified or has had certification revoked for any reason.

(B) The Aggregator is responsible for all local and long distance usage charges billed to the CPPT Line. These charges included, but are not limited to, any operator charges for calls billed to the line on a collect or third party basis in the event that the Aggregator does not subscribe to blocking and screening features offered in Section 5.10.4 of this tariff.

(C) Unless otherwise permitted by Commission rule or order, only one Pay Telephone instrument may be connected to each CPPT line.

(D) Unless otherwise permitted by Commission rule or order, 0- local operator assisted calls must be routed to the Company's operators.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.7 Access Lines for Customer Provided Pay Telephones, (Cont'd.)

(E) Aggregators subscribing to the Company's CPPT Lines are responsible for compliance with the Commission's "Regulations for Operator and Pay Telephone Services" and any other rules or regulations the Commission may require.

7.7.3 Rates and Charges

Service is provided at Business Flat Rate Local Exchange Service rates and charges as specified in Section 7.3 of this tariff. Each Access Line is provided with touch-tone signaling at no additional charge. Calls placed to Directory Assistance from CPPT Lines will be billed to the Customer at rates arid charges found in Section 8.4 of the tariff.

7.7.4 Optional Features

The following optional features are provided with One Source Access Line service:

(A) Unrestricted Service: No blocking or screening provided.

| | |
|---|---|
| Unrestricted. Per Outward Line | $ N/C |
| Unrestricted, Per Two-Way Line | $ N/C |

(B) Screening Option ~A: With this option, an Access Line is equipped with operator screening. In addition, calls to 011+ international direct distance dialed numbers outside the North American Numbering Plan are blocked.

| | |
|---|---|
| Screening Option A, Per Outward Line | $2.85 |
| Screening Option A, Per Two-Way Line | $2.85 |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.7 Access Lines for Customer Provided Pay Telephones, (Cont'd.)

7.7.4 Optional Features (Cont'd.)

(C) Screening Option –B: With this option, an Access Line is equipped with operator screening, blocking of calls to 0111- international direct distance dialed numbers outside the North American Numbering Plan are blocked, and blocking of calls to 900/976, seven digit local, 1+ Expanded Local Calling Area, and 1+ DDP.

| | |
|---|---|
| Screening Option B, Per Outward Line | $3.80 |
| Screening Option B, Per Two-Way Line | $3.80 |

(D) Screening ~ With this option, an Access Line is equipped with operator screening, blocking of calls to 011+ international direct distance dialed numbers outside the North American Numbering Plan are blocked, and blocking of calls to 900/976, and 1+ Expanded Local Calling Area.

| | |
|---|---|
| Screening Option C, Per Outward Line | $2.85 |
| Screening Option C, Per Two-Way Line | $2.85 |



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SECTION 7 –LOCAL EXCHANGE SERVICES (CONT'D)

7.8 Optional Calling Features

The features in this section are made available on an individual basis or as part of multiple feature packages. All features are provided subject to availability. Certain features may not be available with all classes of service. Transmission levels for calls forwarded or calls placed or received using optional calling features may not be acceptable for all some uses iii some cases.

7.8.1 Features Offered on a Usage Sensitive Basis

The following features arc available to all local exchange Business and Residence line Customers where facilities and services permit. Customers may utilize each feature by dialing the appropriate access code. The Customer will be billed the Per Feature Activation Charge shown in the following table each time a feature is used by the Customer. Customers may subscribe to these features on a monthly basis at their option to obtain unlimited use of these features for a fixed monthly charge.

| | Bellsouth Service Areas | | Verizon Service Areas | |
|---|---|---|---|---|
| Optional Features | Residence | Business | Residence | Business |
| Three-Way Calling | 0.90 | 0.90 | 0.75 | 0.75 |
| Call Return | 0.90 | 0.90 | 0.75 | 0.75 |
| Repeat Dialing | 0.90 | 0.90 | 0.75 | 0.75 |

Denial of per call activation for Three-Way Calling, Call Return and Repeat Dialing from any line or trunk is available to Customers upon request at no additional charge.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.8 Optional Calling Features, (Cont'd.)

7.8.2 Features Offered on Monthly Basis

The following optional calling features are offered to Customers on a monthly basis. Customers are allowed unlimited use of each feature. No usage sensitive charges apply. Multiline Customers must order the appropriate number of features based on the number of lines which will have access to the feature.

A. Bellsouth Service Areas

| Optional Calling Feature | Residence | Business |
|---|---|---|
| Call Forwarding Variable | 4.00 | 6.00 |
| Call Forwarding Variable with Remote Access | 6.50 | 8.00 |
| Call Forwarding Don't Answer – Basic | 1.50 | 2.95 |
| Call Forwarding Don't' Answer with Ring Control | 1.50 | 3.50 |
| Call Forwarding Don't' Answer with Customer Control | 4.00 | 7.00 |
| Call Forwarding Busy Line – Basic | 1.50 | 2.95 |
| Call Forwarding Busy Line w/Customer Control | 3.50 | 7.00 |
| Call Waiting – Basic | 4.50 | 7.00 |
| Call Waiting – Deluxe | 6.50 | n/a |



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# SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

## 7.8 Optional Calling Features, (Cont'd.)

### 7.8.2 Features Offered on Monthly Basis (Cont'd)

#### A. Bellsouth Service Areas (Cont'd)

| Optional Calling Feature (cont'd) | Residence | Business |
|---|---|---|
| Caller ID- Basic | 5.00 | 11.00 |
| Caller ID – Deluxe | 7.95 | 11.00 |
| Caller ID- Deluxe w/ ACR | 7.95 | 11.00 |
| Anonymous Call Rejection (ACR) | 3.00 | 4.00 |
| Call Block | 5.00 | 6.50 |
| Call Return | 5.00 | 6.50 |
| Call Tracing | 5.00 | 6.50 |
| Calling Number Delivery Blocking (per line equipped) | 3.50 | n/a |
| Message Waiting Indication – Audible | 0.50 | 0.50 |
| Message Waiting Indication – Audible and Visual | 0.50 | 0.50 |
| Multiple Directory Number Distinctive Ringing – First DN | 4.00 | 8.00 |
| Multiple Directory Number Distinctive Ringing – Second DN | 6.00 | 11.00 |
| Preferred Call Forwarding | 5.00 | 6.50 |
| Repeat Dialing | 5.00 | 6.50 |
| Speed Dialing (30 codes) | 5.00 | 5.00 |
| Speed Dialing (8 codes) | 4.50 | 5.00 |
| Three Way Calling | 5.00 | 6.50 |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.8 Optional Calling Features, (Cont'd.)

7.8.2 Features Offered on Monthly Basis (Cont'd)

A. Verizon Service Areas

| Optional Calling Feature | | Residence | Business |
|---|---|---|---|
| Call Waiting | | 3.70 | 5.50 |
| Cancel Call Waiting | | 1.00 | 2.00 |
| Call Forwarding (Variable) | | | |
| | Standard | 3.50 | 4.50 |
| | Multipath[1] | 3.50 | 4.50 |
| Speed Calling | | | |
| | 8-Number | 2.50 | 3.50 |
| | 30-Number | 3.50 | 5.00 |
| Three-Way Calling | | 3.75 | 5.00 |
| Distinctive Ring, each line | | 6.00 | 6.00 |
| VIP Alert | | 3.00 | 4.00 |
| Call Tracing | | 5.00 | 6.00 |
| Complete Blocking | | 2.00 | 2.00 |
| Toll Denial | | 2.75 | 4.75 |
| Special Call Handling | | | |
| | Acceptance | 3.00 | 4.00 |
| | Forwarding | 5.00 | 6.00 |

[1] Multipath is available only as an enhancement to Call Forwarding.



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.8 Optional Calling Features, (Cont'd.)

7.8.2 Features Offered on Monthly Basis (Cont'd)

A. Verizon Service Areas (Cont'd)

| Optional Calling Feature (Cont'd) | Residence | Business |
|---|---|---|
| Automatic Busy Redial | 5.00 | 6.00 |
| Call Block | 3.00 | 4.00 |
| Anonymous Call Reject (ACR) | 1.00 | 1.00 |
| Caller ID Number with ACR | 7.00 | 10.00 |
| Caller ID Name & Number with ACR | 7.95 | 11.50 |
| Automatic Call Return | 5.00 | 6.00 |
| Non-Published Service | 2.30 | 2.30 |
| Non-Listed Service | 2.30 | 2.30 |
| Additional Listings, each | 1.00 | 1.20 |
| Per Use Local Features | | |
| Automatic Call Return | 0.75 | 0.75 |
| Busy Redial | 0.75 | 0.75 |
| Three-Way Calling | 0.75 | 0.75 |



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SECTION 7 – LOCAL EXCHANGE SERVICES (CONT'D)

7.8 Optional Calling Features, (Cont'd.)

7.8.3 Multiple Feature Discounts – Bellsouth Service Areas Only

Customers may receive a per line discounts in the form of a credit on their bill based on the total number of features subscribed to for each line at the end of a given billing period.

| Number of Features | Residence Discount | Business Discount |
|---|---|---|
| 2 | 0.15 | 0.50 |
| 3 | 0.35 | 1.00 |
| 4 | 0.55 | 1.50 |
| 5 | 0.75 | 2.00 |
| 6 | 0.75 | 2.00 |
| 7 | 0.75 | 2.00 |
| 8 | 0.75 | 2.00 |
| 9 | 0.75 | 2.00 |



Ross McApline, President
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Phoenix, Arizona 85040
Phone Number: (602) 253-6004, E-Mail Address: jon_brinton@inter-tel.com

7.8 Optional Calling Features, (Cont'd.)

7.8.4 Multiple Feature Packages – Verizon Service Areas Only

A. Feature Package Option B

Call Waiting, Cancel Call Waiting, Call Forwarding, Three-Way Calling, *69 & Call Block

Residence Service Only............................................... $ 9.00

B. Feature Package Option A

Call Waiting, Cancel Call Waiting, Call Forwarding, Three-Way Calling, Speed Dailing-8, Distinctive Ring, Caller ID, Anonymous Call Block, Call Waiting ID[1], Busy Redial, *69, Call Block, Do Not Disturb, Select Call Forwarding, & Priority Call

Residence Service Only............................................... 16.00

[1] Where available.



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7.8 Optional Calling Features, (Cont'd.)

7.8.4 Multiple Feature Packages – Verizon Service Areas Only (Cont'd)

C. Business Feature Choice Local Feature Package

1. Business Feature Choice service offers a discount when the customer subscribes to three or more calling services as specified in b. following. If the number of services ordered is less than three or the customer removes a service or services such that the total subscribed to becomes less than three, the discount does not apply and the individual applicable rates apply. The service is available to single line business customers.

2. The following services are available for the Business Feature Choice offering:

| | |
|---|---|
| Busy Redial | Do Not Disturb |
| *69 | Select Call Forwarding |
| Call Block | Speed Dialing 8 |
| Call Forwarding | Speed Dialing 30 |
| Call Waiting/Cancel Call Waiting | Three-Way Calling |
| Caller ID | Priority Call |
| Caller ID – Number Only | Distinctive Ring |

3. The following discount applies when a customer subscribes to three or more qualifying company calling services:

Business Service 30 % Discount



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## CERTIFICATE OF SERVICE

The undersigned employee of Elliott & Elliott, P.A. does hereby certify that she has served below listed parties with a copy of the pleading(s) indicated below by mailing a copy of same to them in the United States mail, by regular mail, with sufficient postage affixed thereto and return address clearly marked on the date indicated below:

RE: Application of Inter-tel Netsolutions, Inc. for a Certificate of Public Convenience and Necessity to Provide Local Exchange Telecommunications Services and for local service offerings to be regulated in accordance with procedures authorized for NewSouth Communications in Order No. 98-165 in docket No. 97-467-C

PARTIES SERVED: C. Dukes Scott, Esquire
Office of Regulatory Staff
PO Box 11263
Columbia, SC 29211

PLEADING: Application of Inter-tel Netsolutions, Inc. for Authority to Provide Resold and Facilities-based/UNE Local Exchange Service

April 19, 2007

Marcia W. Walters

Marcia W. Walters, Legal Assistant

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